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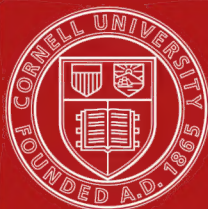
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A treatise on the law of stock and stock



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A TREATISE
ON THE
LAW OF
STOCK AND STOCKHOLDERS

AS APPLICABLE TO
RAILROAD, BANKING, INSURANCE, MANUFACTURING,
COMMERCIAL, BUSINESS, TURNPIKE, BRIDGE, CANAL,
AND OTHER PRIVATE CORPORATIONS.

BY WILLIAM W. COOK,
OF THE NEW YORK BAR.

NEW YORK:
BAKER, VOORHIS & CO., LAW PUBLISHERS,
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1887.

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By WILLIAM W. COOK.

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TO
THE HONORABLE
THOMAS M. COOLEY, LL.D.,
PROFESSOR, AUTHOR, AND JUDGE,
WHOSE PRE-EMINENT ABILITY, UNTIRING RESEARCH,
PROFOUND LEARNING, AND EXALTED CHARACTER,
HAVE SECURED FOR HIM
AN IMPERISHABLE FAME AS A JURIST,
UNDER WHOSE INSTRUCTION THE AUTHOR ACQUIRED A DESIRE TO SEARCH OUT
AND MASTER THE PRINCIPLES OF THE LAW,
THIS WORK
IS
RESPECTFULLY DEDICATED.

PREFACE.

The remarkably rapid growth of corporations during the past twenty-five years has created a body of law which is fast becoming a system of jurisprudence in itself. This system has become so vast, complicated, and unwieldy that it is believed that the time has come when a thorough treatment of the subject requires a division of it into many parts. To a large extent this division has already been accomplished. As regards the important subject of Stock and Stockholders, however, there has been a singular deficiency in the text-books, and a study of the cases has led the writer to a realization of the fact that no single treatise attempts to treat of the principles of law relative to that subject. It was in consequence of this fact, and because the need of a treatise on the subject of Stock and Stockholders has been clearly felt and often manifested, that this work was undertaken.

It is not, however, the result of a preconceived idea as to the scope, divisions, and limits of the subject. The subject itself, in its extent and plan, has been a matter of growth in the author's mind. It was found that many of the most important and practical principles governing stocks had never been investigated and presented by law writers. Particularly was this true as regards fictitiously paid-up stock, commonly called "watered" stock, legacies of stock, life-estates and remainders in stock, methods of issuing stock, the law regulating corporate rights in allowing or refusing a registry of transfers, the risks incurred in purchasing certificates of stock, pledges of stock, taxation of stock, joint-stock companies, and frauds of directors. It was found also that

PREFACE.

many of the other subjects herein had been only partially investigated by the text-book writers, or had been dismissed with a bare reference, as illustrating general principles of corporation law.

The plan of the work is original, and this volume is the result of a long and conscientious study of the sources of authority—the cases themselves. These have been systematically examined and collected, and made the groundwork of the limits and subdivisions of the work. Nevertheless the text-books on the various branches of corporation law have not been neglected, but in the preparation of the work, the writer has consulted them, and he fully appreciates their excellence, learning, and intrinsic worth.

The writer has sought to make a clear, practical, and complete presentation of the subject for the every-day use of the bench and bar. The divisions of the treatise, the chapter subjects, and the section headings, are so made as to aid in finding, without delay, the point of law in which any one may be interested. These divisions and headings have been built up from the cases themselves, and from a study of the subjects which arise most frequently in the courts and in business transactions. The writer has carefully avoided all theories, long discussions, and, as far as possible, the use of technical language. He has not hesitated to express his opinion when the occasion seemed to warrant it, but his sole object has been to give a complete and concise statement of the law governing the subject of Stock and Stockholders.

A special effort has been made to develop fully those subjects which are most often litigated in our courts, and which occasion doubt, difficulty, danger and law suits to corporations and stockholders. The number and complexity of the decisions have caused some confusion and doubt, even in the mind of the bench itself. Out of the chaos of material which lay scattered throughout many thousands of reports, the writer has sought to construct a treatise that will be a practical guide on all subjects

PREFACE.

relative to stocks, which are of importance and constant interest and use to lawyers, investors, directors, stockholders, corporations and the general public.

Copious notes are given for the purpose of illustrating, fortifying, and explaining the text. By this method it is believed that the thread of the subject is preserved in the text and the mind of the reader not distracted by a mass of details. On the other hand, by the notes, the subject is still farther developed and the application of the principles to particular facts fully set forth.

The dates of most of the cases are given in the notes. It is believed that thereby the relative importance of a given case can be more easily ascertained and determined. It is also worthy of note that the dates of the cases become of great use when there is a conflict of authority. By the dates also the important facts are brought out that the law of Stock and Stockholders is of very recent origin; that most of the cases have arisen within the past fifty years; that the law relative to stockholders' actions against directors has arisen within thirty years, and that we are as yet only on the threshold of that new jurisprudence which, though now in a formative state, is for the future to regulate the great subject of corporations having a capital stock.

In the composition of this work, the author has been burdened with an abundance, rather than a paucity of material. The law of Stock and Stockholders, when explored in all its branches and details, is a vast subject, and that which was expected to fill a volume of five hundred pages has, with difficulty, been confined to nine hundred pages. There are about six thousand cases cited in this volume, a number which is a surprise even to the writer himself. Although it is difficult to exhaust, in a single volume, the law contained in so great a number of cases, yet a conscientious effort has been made to that end, in so far as these cases bear upon the subject.

In the final preparation of the sheets for the press, I have received valuable suggestions and assistance from my friend

PREFACE.

CHARLES F. BEACH, Jr., Esq. (the author of the work on "Contributory Negligence"), to whom I extend my thanks.

If my work shall prove to be of use to the profession, I shall feel amply compensated. Although this book has received my unremitting attention and anxious care for several years, in order to render it trustworthy, yet the multiplicity and difficulty of the questions which it treats and the large number of cases which have been examined, studied, condensed, and stated, are such as to forbid the hope that I have always avoided error or that the work is free from faults. Trusting however that it may be found to have merits, it is submitted, with diffidence, to the judgment of a candid and discriminating, yet generous profession.

WILLIAM W. COOK.

115 BROADWAY, NEW YORK,
January 12th, 1887.

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THE LAW
OF
STOCK AND STOCKHOLDERS.

STOCK AND STOCKHOLDERS.

PART I.

ISSUE OF AND LIABILITY ON STOCK.

CHAPTER I.

INTRODUCTORY.—OF STOCK AND STOCKHOLDERS GENERALLY.

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| § 1. Classes of corporations and the class considered herein. | § 6. Shares are personalty and not real property. |
| 2. Corporations having a capital stock. | 7. Stock as property. |
| 3. Definition of capital stock. | 8. Law of place governing stock. |
| 4. Definition of corporator, subscriber, shareholder, and stockholder. | 9. Classes of stock. |
| 5. Shares of stock defined. | 10. Certificates of stock. |

§ 1. *Classes of corporations and the class considered herein.*

—A corporation, as defined by Chief Justice Marshall in the Dartmouth College case,¹ is ‘an artificial being, invisible, intangible, and existing only in contemplation of law.’ This felicitous definition comprehends incorporated bodies of every class and nature. For the better understanding, however, of the law of corporations, and for the treatment of special branches of that law, the early writers, like Kyd, Blackstone, Kent, Angell, and Ames, and many subsequent authors, have subdivided corporations into distinct classes. These subdivisions have been made on various principles of classification. When divided with respect to the members of corporations, they are aggregate and sole. As regards their functions, they are public or municipal, and private; and again, private corporations are divided into ecclesiastical or religious, and lay; and still further, lay corporations are divided into eleemosynary or charitable, and civil, which include all private corporations that are created for temporal purposes, such as banking, insurance, trading, railroad, manufacturing, turnpike, bridge, and canal corporations. Civil corporations include also certain public corporations, such as municipalities, and certain

¹ Dartmouth College v. Woodward, 4 Wheat. 518, 636 (1819).

educational institutions. At an early day, private corporations for business purposes were few in number and of little importance in the law. Chancellor Bland states that no instance of such a corporation in the colonial times of America can be found.¹ In England, also, at that time, private corporations for profit were of small consequence. But the past seventy-five years have completely reversed the relative importance of the different classes of corporations, and, at the present time, private corporations for temporal purposes have completely overshadowed all other kinds.

With this change there is a decided tendency to re-classify the subject, and the modern treatises on corporation law have recognized the fact that old classifications are to be disregarded, and that corporations are to be divided into joint-stock corporations, or those having a capital stock, and corporations without a capital stock.² This classification is due largely to the remarkable growth of the law regulating the one prominent difference between the two classes. That feature is that corporations with a capital stock have stock and stockholders, while corporations without a capital stock have none, but are governed largely by principles of law that have changed little since the days of Blackstone and Kent. It is with this feature of modern corporations, as distinguished from those that especially characterized the early corporations at common law, and that have sunk into comparative unimportance,³ that the present work is concerned.

§ 2. *Corporations having a capital stock.*—This treatise, however, does not discuss all the questions which arise in connection with corporations having a capital stock. In some respects this class of corporations involves principles of law in common with corporations which have not a capital stock. The old questions of how a corporation shall contract; whether a seal be necessary; the right to appear by attorney; the power to make

¹ McKim v. Odom, 3 Bland's Ch. (Md.) 407, 418 (1828).

² The recent work of Taylor on "Corporations having a Capital Stock" bears witness to this fact; as does also Morawetz on Corporations, a work which treats very little of the older classes of corporations and the principles which govern them, but fully and clearly of private corporations having a capital stock. It is well to state here that a joint-stock corporation and a joint-stock company are essentially different. Both have a capital

stock, and both are managed by boards of officers and meetings of the stockholders. But a joint-stock company is unincorporated and is but a partnership. See Chapter on Joint-Stock Companies.

³ The subject of municipal corporations would seem to form an exception to this statement, were it not that the great and deservedly successful work of Judge Dillon on Municipal Corporations has clearly stated and thereby settled most of the difficult subjects connected with that branch of the law.

by-laws; the right to sue and be sued; and to hold and dispose of property in the corporate name, are questions, capacities, and incidents common to all corporations, and for the most part have become so well settled as to give rise to comparatively little litigation at the present day. On the other hand it is believed that the modern law of corporations, as regards its litigated questions, its unsettled principles, and its rapidly crystallizing results, is centered largely on two subjects—the law of express and implied corporate powers,¹ and the law of stock and stockholders. The latter is the subject of this treatise.

§ 3. *Definition of capital stock.*—Capital stock is the sum fixed by the corporate charter as the amount paid in or to be paid in by the stockholders, for the prosecution of the business of the corporation, and for the benefit of corporate creditors in case the corporation becomes insolvent.² The capital stock is to be clearly distinguished from the amount of property possessed by the corporation. Occasionally, under the terms of taxation statutes, which have been drawn without regard to the technical meaning of words, the courts will construe the capital stock to mean all the actual property of the corporation.³ But this is for the purpose of carrying out the intent of the statute, and is not the real meaning of the term. At common law the capital stock does not

¹ This is evidenced by the popularity and constant demand and use of that learned work, Green's Brice's *Ultra Vires*; also by the treatises on railroad law by Rorer, Wood, Pierce, Redfield, and Sheldford, works which treat largely of the powers of railroads to contract, to take land, &c. So also a mere cursory view of the numerous decisions on corporation law by the courts at the present day, will show that these two subjects constitute the kernel of modern corporation litigation.

² For various definitions see *Barry v. Merchants' Ex. Co.*, 1 Sand. Ch. 280-305 (1844); *Hightower v. Thornton*, 8 Ga. 486, 500 (1850); *Hannibal & St. J. R. R. Co. v. Shacklett*, 30 Mo. 551, 558 (1860); *St. Louis Iron M., &c., R. R. Co. v. Loftin*, 30 Ark. 693, 709 (1875); *Bent v. Hart*, 10 Mo. App. 143-146 (1881); *Mutual Ins. Co. v. Supervisors, &c.*, 4 N. Y. 442 (1851); *Bailey v. Clark*, 21 Wall. 284 (1874); where Field, J., says "it applies only to the property or means contributed by the stockholders as the fund or basis for

the business or enterprise for which the corporation or association was formed." *Jones v. Davis*, 35 O. St. 474, 476 (1880); *Burrall v. Bushwick R. R. Co.*, 75 N. Y. 211 (1878), where Folger, J., defines it as "that money or property which is put in a single corporate fund by those who by subscription therefor become members of a corporate body." *Williams v. Western Union Tel. Co.*, 93 N. Y., 162-188 (1883), where Earl, J., tersely says it is "the property of the corporation contributed by its stockholders or otherwise obtained by it, to the extent required by its charter." *Sanger v. Upton*, 91 U. S. 56, 60 (1875); *State v. Morristown Fire Assn.*, 23 N. J. L. 195; *State v. Cheraw & C. R. R. Co.*, 16 S. C. 524 (1881).

³ *Ohio & M. R. R. Co. v. Weber*, 96 Ill. 443 (1880); *City of Philadelphia v. Ridge Ave. R. R. Co.*, 102 Penn. St. 190 (1880). In valuation for purposes of taxation it has been held that the value of the charter is not to be included as a part of the capital stock. *Coit v. North C. Gold A. Co.*, 14 Fed. Rep. 12 (1882).

vary, but remains fixed, although the actual property of the corporation may fluctuate widely in value and may be diminished by losses or increased by gains. The term "stock"¹ has been used at times to indicate the same thing as capital stock. Generally, however, it means shares of stock, and in this sense it is used in this treatise.

§ 4. *Definitions of corporator, subscriber, shareholder, and stockholder.*—A corporator is one of those to whom a charter is granted, or of those who file a certificate of incorporation under a general incorporating statute.² A subscriber is one who has become liable to the corporation for one or more shares of stock in the corporation.³ A shareholder in this country means the same thing as a stockholder, and the terms are used interchangeably to indicate one who owns stock in a corporation and has been accepted as a stockholder by the corporation.⁴ A stockholder does not stand in the attitude of a partner towards the corporation.

¹ *Burr v. Wilcox*, 22 N. Y. 551-555 (1860); *People v. Commissioners, &c.*, 23 N. Y. 192-220 (1861); *Bailey v. Railroad Co.*, 22 Wall. 604-637 (1874).

² *Chase v. Lord*, 77 N. Y. 1-11 (1879), the court saying: "Corporators exist before stockholders, and do not exist with them. When stockholders come in, corporators cease to be." *Cf. Lady Bryan's Case*, 1 Sawy. 349. That promoters or corporators need not be subscribers to the stock of the company, see *Densmore Oil Co. v. Densmore*, 64 Penn. St. 43, 54 (*Sharswood, J.*) (1870).

³ *Busey v. Hooper*, 35 Md. 15, holding that a subscriber is not a stockholder, but is only in position to become one. *Spear v. Crawford*, 14 Wend. 20-23 (1835). In England it has been held that under a statute the subscriber must sign the incorporation articles and by-laws before he can become a stockholder. *Wilkinson v. Anglo-Col. Gold M. Co.*, 18 Q. B. 728 (1852). See also Chap. IV.

⁴ See *Rosevelt v. Brown*, 11 N. Y. 148-150 (1854), holding that so far as corporate creditors are concerned, the stockholders need not be the stockowners. *State v. Ferris*, 42 Conn. 560 (1875); *Adderly v. Storm*, 6 Hill, 624 (1844); *Worrall v. Judson*, 5 Barb. 210 (1849). Where the registered holder is merely a nominal holder, he will not be entitled to special privileges, such as free admission to a place of amusement. *Appeal*

of *American Acad., &c. (Penn.)*, 2 East. Rep. 386 (1885). In behalf of corporate creditors, where the corporation is insolvent, a person is often held to be a stockholder, although no certificate has been issued to him, and the ordinary *indicia* of stockholdership do not indicate that he is a stockholder. *Sanger v. Upton*, 91 U. S. 56 (1875); *Upton v. Tribilcock*, 91 U. S. 45 (1875); *Wheeler v. Miller*, 90 N. Y. 353 (1882); *Burr v. Wilcox*, 22 N. Y. 55 (1860); *Slee v. Bloom*, 19 Johns. 456 (1822); *Dorris v. French*, 4 Hun, 292 (1875); *Hamilton, &c., R. R. Co. v. Rice*, 7 Barb. 157-167 (1849); *Clark v. Farrington*, 11 Wis. 306, 327 (1860); *Haynes v. Brown*, 36 N. H. 545-563 (1858); *Chesley v. Cummings*, 37 Me. 76-83 (1853); *Chester, &c. v. Dewey*, 16 Mass. 94 (1819); *Griswold v. Seligman*, 72 Mo. 110; *Schaffer v. Mo. & Co.*, 46 Mo. 248 (1870); *Boggs v. Olcott*, 40 Ill. 303 (1866); *Re South Mountain, &c.*, 7 Sawy. 20 (1881); *Upton v. Burnham*, 3 Biss. 431 (1873); *Johnson v. Albany, &c., R. R. Co.* 40 How. Pr. 193; *New Albany, &c., R. R. Co. v. McCormick*, 10 Ind. 499 (1838); *Payne v. Elliot*, 54 Cal. 339 (1880). In *Griswold v. Seligman*, 72 Mo. 110 (1880), the court says: "Our statute make a clear distinction between mere stockholders and stockowners. . . . It is stockowners only who can be made liable for the debts of the corporation."

He may sue the corporation, or be sued by it, both at law and in equity.¹ Moreover, he has a direct interest in the corporation, and at times may take the part of the corporation in prosecuting or defending its suits.² A shareholder in a corporation, which does not properly insure its property, has such an insurable interest in that property that he may recover upon a policy thereon taken in his own name, for an amount which, added to the company's insurance, would cover his interest.³

At common law the stockholder, on account of his interest in the corporation, was not a competent witness in a suit in which the corporation was a party. In some States, however, this rule has been changed by statute, and in others it is easily evaded by a formal transfer of the certificate of stock to another person.⁴

A stockholder is incompetent to serve as a judge⁵ or juror⁶ in

¹ *Waring v. Cahawba Co.*, 2 Bay (S. C.), 109 (1797), where this right of a stockholder was the question in litigation. *Rogers v. Danby Univ. Soc.*, 19 Vt. 187 (1847); *Culberston v. Wabash Nav. Co.*, 4 McLean, 544 (1849); *Peirce v. Partridge*, 44 Mass. 44 (1841); *Barnstead v. Empire Min. Co.*, 5 Cal. 299 (1855); *Ex parte Booker*, 18 Ark. 338 (1857). A stockholder as a creditor of the corporation may obtain security for his debt in exclusion of other creditors. *Reichwald v. Commercial Hotel Co.*, 106 Ill. 439 (1883).

² See Part IV.

³ *Warren v. Davenport Fire Ins. Co.*, 31 Iowa, 464 (1871); distinguishing *Phillips v. Knox County Ins. Co.*, 20 Ohio, 174 (1851); cf. *Seaman v. Enterprise Fire, &c., Ins. Co.*, 18 Fed. Rep. 250; s. c. 5 McCrary, 558 (1883). *Contra*, *Riggs v. Commercial, &c., Ins. Co.*, 51 N. Y. Super. Ct. 466 (1884). See *Greenhood on Public Policy*, 255; *Angell on Fire & Life Insurance*, Chap. XI, and cases cited.

⁴ See N. Y. Code of Civil Procedure, §§ 828, 839. That a transfer will render the transferer competent, see *Ill. Ins. Co. v. Marseilles Mfg. Co.*, 6 Ill. 236 (1844); *Union Bk. v. Owen*, 4 Humph. (Penn.) 338 (1843); *Bell v. Hull*, 6 M. & W. 699 (1840); 1. Greenleaf's Evidence, § 429. He is competent though the transfer has not been registered. *Bank of Utica v. Smalley*, 2 Cow. 770 (1824); *Gilbert v. Manchester Iron Mfg. Co.*, 11 Wend. 627 (1834); *Delaware, &c., R. R. Co. v. Irick*, 23 N. J. L. 321 (1852); and

although he expects to buy it back, provided there is no agreement expressly to that effect. *Utica Ins. Co. v. Cadwell*, 3 Wend. 296 (1829); *State v. Catskill Bk.*, 18 Wend. 466 (1837).

⁵ *Dinns v. Prop. of Grand Junction Canal*, 3 H. L. Cases, 759 (1852), where the Lord Chancellor was a stockholder in the defendant company, and had affirmed a decree by the Vice-Chancellor in the case. The House of Lords reversed the decision on this ground. *Cooley on Constitutional Limitations*, §§ 410, 411; *Washington Ins. Co. v. Price*, 1 Hopk. Ch. (N. Y.) 1 (1823), Chancellor Sandford therein refusing to follow Chancellor Kent in *Stuart v. Mechanics & Farmers Bk.*, 19 Johns. 496-501 (1822). In *Peninsular Ry. Co. v. Howard*, 20 Mich. 18 (1870), the court says: "It is not a matter of discretion with the judge or other person acting in a judicial capacity, nor is it left to his own sense of propriety or decency, but the principle forbids him to act in such capacity at all, when he is thus interested or when he may possibly be subjected to the temptation."

⁶ *Page v. Contocook Valley R. R. Co.*, 21 N. H. 438 (1850); *Peninsular R. R. Co. v. Howard*, 20 Mich. 18 (1870); *Fleeson v. Savage S. M. Co.*, 3 Nev. 157 (1867); *Silver v. Ely*, 3 Watts & S. (Penn.) 420 (1842). Cf. *Williams v. Smith*, 6 Cow. 166 (1826). The incompetency extends to the son of a stockholder. *Georgia R. R. Co. v. Hart*, 60 Ala. 550 (1878). A person donating to the railroad is incompetent to serve in condemnation proceedings. *Michigan Air Line Ry. Co.*

a case in which the corporation is a party. A director need not necessarily be a stockholder, unless a statute or the charter expressly so provides.¹

§ 5. *Shares of stock defined.*—A share of stock may be defined as a right which its owner has in the management, profits, and ultimate assets of the corporation. By the Court of Appeals of New York it is said that “the right which a shareholder in a corporation has, by reason of his ownership of shares, is a right to participate according to the amount of his stock in the surplus profits of the corporation on a division, and ultimately on its dissolution, in the assets remaining after payment of its debts.”²

Chief Justice Shaw, by way of a definition of a share of stock, says: “The right is, strictly speaking, a right to participate in a certain proportion, in the immunities and benefits of the corporation, to vote in the choice of their officers, and the management of their concerns, to share in the dividends of profits, and to receive an aliquot part of the proceeds of the capital, on winding up and terminating the active existence and operations of the corporation.”³ It is said that the rights which a share of stock secures to its owner, are the rights “to meet at stockholders’ meetings, to participate in the profits of the business, and to require that the corporate property shall not be diverted from the original purpose.”⁴ An English case has said: “It is cer-

v. Barnes, 40 Mich. 383 (1879). A stockholder is competent though the corporation is interested in a subsequent case on the same facts. *Commonwealth v. Boston, &c., R. R. Co.*, 57 Mass. 25 (1849). Objection to competency must be raised at the trial. It cannot be raised for first time by motion for new trial. *Williams v. Great Western Ry. Co.*, 3 H. & N. 869 (1859). A stockholder may be the receiver or assignee of the corporation. *Covert v. Rogers*, 38 Mich. 363 (1878).

¹ *Wight v. Springfield, &c., R. R. Co.*, 117 Mass. 226 (1875); *Re St. Lawrence Steamboat Co.*, 44 N. J. L. 529-541 (1882); *State v. McDaniel*, 22 O. St. 354 (1872). *Cf. Bartholomew v. Bentley*, 1 O. St. 37 (1852); *Despatch Line v. Bellamy Mfg. Co.*, 12 N. H. 205-223 (1841); *Cumming v. Prescott*, 2 Younge & C. 488 (1837); *Stack’s Case*, 33 L. J. (Ch.) 731 (1864).

² *Plimpton v. Bigelow*, 93 N. Y. 592, 599 (1883). To same effect see *Burrall v. Bushwick R. R. Co.*, 75 N. Y. 211, 216

(1878); *Kent v. Quicksilver Mining Co.*, 78 N. Y. 159 (1879); *Jermain v. Lake Shore, &c., R. R. Co.*, 91 N. Y. 483-492 (1883); *Field v. Pierce*, 102 Mass. 253, 261 (1869); *Jones v. Davis*, 35 Ohio St. 474, 477 (1880); *Bradley v. Bauder*, 36 Id. 28, 35 (1880); *Bent v. Hart*, 10 Mo. App. 143 (1881); *Harrison v. Vines*, 46 Texas, 15, 21 (1876); *Brightwell v. Mallory*, 10 Yerg. (Tenn.) 196 (1836); *Barksdale v. Finney*, 14 Gratt. 338, 357 (1858); *Van Allen v. Assessors*, 3 Wall. 573, 585 (1865).

³ *Fisher v. The Essex Bk.*, 5 Gray, 373, 378 (1855). *Cf. Arnold v. Ruggles*, 1 R. I. 165 (1837).

⁴ *Forbes v. Memphis, &c., R. R. Co.*, 2 Woods, 323, 331 (1872). *Cf. Payne v. Elliott*, 54 Cal. 339 (1880). Mr. Justice Sharswood says: “A share of stock is an incorporeal intangible thing. It is a right to a certain proportion of the capital stock of a corporation—never realized except upon the dissolution and winding up of the corporation—with the right to receive in

tainly not easy to define precisely the meaning of 'stock.' It is not an ancient subject of property, nor known to the common law. It is, however, a hereditament. It is an annuity and treated as such by act of parliament."¹

Hence it may be concluded that a share of stock is a proportional part of certain rights in the management and profits of the corporation during its existence, and in the assets upon dissolution.²

§ 6. *Shares are personalty and not real property.*—With reference more particularly to the essential nature of shares of stock, it has been well settled that such property is personalty and not realty. It is said that a share of stock is not real estate, has nothing to give it the character of real estate, is not land, nor an hereditament, nor an interest in either of them.³ In some of the earlier

the meantime such profits as may be made and declared in the shape of dividends." *Neiler v. Kelley*, 69 Penn. St. 403, 407 (1871). In one of the earliest English cases in point, *Wildman v. Wildman*, 9 Vesey, 174, 177 (1803), it was said by Grant, M. R., that: "The interest in stock is properly nothing but a right to receive a perpetual annuity, subject to redemption."

¹ *The King v. Capper*, 5 Price (Eng. Exch.), 217, 262 (1817).

² *Oakbank Oil Co. v. Crum*, L. R., 8 App. Cas. 65 (1882). In England, there are certain terms used, which are peculiar to that country, and have a meaning other than their meaning in this country. Thus scrip is a written acknowledgment by a corporation, that the holder will be entitled to certain shares of stock and a certificate, therefor, when the unpaid installments on such shares are all paid in. They are negotiable instruments. *Goodwin v. Roberts*, L. R., 1 App. Cas. 476 (1876); *Rumball v. Metropolitan Bk.*, L. R., 2 Q. B. Div. 194 (1877). Stock "is a fund or capital, which is capable of being divided into, and held in any irregular amount. Thus, the ordinary government funds (consols, new threes, &c.) are called 'stocks,' because a person can buy them in any amount (such as £99, 19s. 11d. as well as £100). A share or debenture, on the other hand, is of a fixed amount (such as £10, £50, £100), and is incapable of subdivision or consolidation." *Rapalje & Lawrence's Law Dic.* p. 1224. Shares may be converted by the company into

stock, so as to enable their holders to dispose of them in small or irregular amounts. *Hurrell & Hyde on Joint Stock Companies*, 47. An English debenture is very much the same as an American mortgage on corporation property. Debenture stock differs from a pure debenture, in that the title of each original holder appears in a registry, instead of being represented by an instrument complete in itself, and the stock is capable of being transferred in any amounts, unless limited by corporate regulations. See *Attree v. Hawe*, L. R., 9 Ch. D. 337 (1878). Articles of association are similar to by-laws, and are for the regulation and management of the corporation. Memorandum of association are the same as the American articles of incorporation, required to be filed under general statutes for incorporations. Deed of settlement is a term that was used in England, prior to 1862, to indicate the same as the modern articles of association, and memorandum of association. See *Burrows v. Smith*, 10 N. Y. 550, 555 (1853).

³ *Bligh v. Brent*, 2 Younge & C. (Exch.) 268 (1836); *Edwards v. Hall*, 6 De G., M. & G. 74 (1855); *Bradley v. Holdsworth*, 3 Mees. & W. 422 (1838); *Ex parte Lancaster Canal Navigation Co.*, 1 Dea. & Ch. 411 (1832); *Watson v. Spratley*, 28 Eng. Law & Eq. 507 (1854). In *Allen v. Pegram*, 16 Iowa, 163, 173 (1864), Mr. Justice Dillon says: "Mr. Williams treats of shares in corporations as '*incorporeal, personal property*,' a very neat and accurate designation. *Wms. on Pers. Prop.* 155." See also *Johns v. Johns*, 1 Ohio St.

cases, perhaps upon the theory that the shareholders had a direct interest in the tangible property of the corporation, shares were held to be real estate where the corporate property consisted wholly or chiefly of realty.¹ But as a result of all the authorities, we may say that, in general, all shares, except possibly those of the somewhat unusual class of incorporated companies where lands are vested directly in the individual members, and the management only is in the corporation² are at the present day to be regarded as personalty,³ a view which has frequently found expression in declaratory statutes both in England⁴ and in the various States of the Union.⁵ Stock, though personalty, is not a chattel. This is the learning in the *King v. Capper*,⁶ a case involving a forfeiture *bonarum et castellarum felonum*. It is rather a chose in action; or, as some older authorities declare, property in the nature of a chose in action.⁷ It is, moreover, of such a

350 (1853), *Thurman, J.*; *Arnold v. Rugles*, 1 R. I. 165 (1837); *Dyer v. Osborne*, 11 Id. 321, 325 (1876); *Tippets v. Walker*, 4 Mass. 595, 596 (1808), *Parsons, C. J.*; *Sargent v. Franklin Ins. Co.*, 8 Pick. 90 (1829); *Weyer v. Second National Bank*, 57 Ind. 198 (1877); *Manns v. Brookville National Bank*, 73 Id. 243 (1881); *Seward v. City of Rising Sun*, 79 Id. 351 (1881); *Southwestern R. R. Co. v. Thomason*, 40 Ga. 408 (1869). *Cf. Wheelock v. Moulton*, 15 Vt. 519 (1843); *Russell v. Temple (Mass.)*, 1798, 3 *Dane's Abr.* 108, 109.

¹ This view was taken by the Court of Appeals of Kentucky. *Price v. Price*, 6 Dana, 107 (1838); *Copeland v. Copeland*, 7 Bush, 349 (1870), by *Robertson, C. J.* But as soon as this latter decision was handed down, the legislature passed an act declaring shares of stock in Kentucky to be personal property, thus bringing the courts of that State into line with other common law courts upon this question. In *Meason's Estate*, 4 Watts, 341 (1835), there is to be found a tendency to hold shares in a toll-bridge, real estate. Turnpike stock was held realty in *Welles v. Cowles*, 2 Conn. 567 (1818); *s. p. Knapp v. Williams*, 4 Ves. Jr. 430 (note) (1798). So of canal shares. *Tomlinson v. Tomlinson*, 9 Beav. 459 (1823). *Cf. Buckeridge v. Ingram*, 2 Ves. 652 (1795); *Drybutter v. Bartholomew*, 2 P. Wms. 127 (1723); *The King v. Winstanley*, 8 Price, 180 (1820). *Contra, Walker v. Milne*, 11 Beav. 507 (1849). See also *Sparling v. Parker*, 9 Id. 450 (1846); *Myers v. Perrigal*, 18 L. J. (Chan.) 185 (1849); *s. c.* 21 L. J. (C.

P.) 217 (1852); *Ashton v. Langdale*, 4 Eng. Law & Eq. 80 (1851); *s. c.* 20 L. J. (Chan.) 234, and an interesting discussion of the question in 3 *Dane's Abridgment*, 103 *et seq.* (1824).

² For an instance of such a corporate arrangement see *Buckeridge v. Ingram*, 2 Ves. Jr. 652 (1795), a case involving the nature of shares in the navigation of the River Avon, under the statute 10 Anne.

³ See an essay by *Henry Budd, Jr., Esq.*, of the Philadelphia bar. *Stock—Its nature and transfer—7 Southern Law Review (N. S.)*, 430 (1881).

⁴ 41 Geo. III, chap. 3; *Watson v. Spratley*, 28 Eng. Law & Eq. 507 (1854); *Ex parte Vallance*, 2 Deacon, 354 (1837); *Ex parte Lancaster Canal Navigation Co.*, 1 Dea. & Ch. 411 (1832).

⁵ 1 Rev. Laws of New York, 247; *New York Laws of 1848*, chap. 40, § 8; *New York Laws of 1850*, chap. 140, § 8; *Laws of New Jersey*, 1830, p. 83, § 17; *Code of Virginia*, p. 550, § 21.

⁶ 5 Price (Eng. Exch.), 217 (1817).

⁷ *Wildman v. Wildman*, 9 Ves. 174 (1803); *Howe v. Starkweather*, 17 Mass. 240, 243 (1821); *Hutchins v. State Bank*, 12 Metc. 421, 426 (1847); *Union Bank of Tennessee v. The State*, 9 Yerg. (Tenn.) 490, 500 (1836); *Allen v. Pegram*, 16 Iowa, 163, 173 (1864); *Arnold v. Ruggles*, 1 R. I. 165 (1837); *Slaymaker v. Bank of Gettysburg*, 10 Penn. St. 373 (1849); *Denton v. Livingston*, 9 Johns. 96 (1812); *Chesapeake, &c., R. R. Co. v. Paine*, 29 Gratt. 502, 506 (1877); *Barksdale v. Finney*, 14 Id. 338, 357 (1858);

nature that it cannot ordinarily, either by act of the law or act of its owner, be reduced to possession.¹ It is an English doctrine that shares of stock are not "goods, wares, or merchandise," as those terms are to be understood in construing that section of the Statute of Frauds which requires delivery, payment, or memorandum in writing of a sale thereof.² In this country, however, the courts have taken the opposite view.³ Furthermore, it is said, that shares are not money,⁴ nor are they a security for money,⁵ nor a credit.⁶

§ 7. *Stock as property.*—Certificates of stock are not negotiable instruments. They have sometimes been said to have a *quasi* negotiability, but this phraseology throws little light upon the real character of the transferability of stock. It may be said in general that by the operation of the law of estoppel the purchaser of a certificate of stock, in good faith and for value, may take it free from many claims of previous holders which would be allowed to come in, in the case of a sale of an ordinary chose in action.⁷

Shares of stock, being in the nature of a chose in action, are, at common law, not subject to levy of execution,⁸ but most of the States have enacted statutes whereby stock may be taken by levy of attachment or of execution. This species of property may also be made subject to taxation,⁹ and for purposes of taxation it exists apart from the corporation, the corporate property, the corporate franchises, and the capital stock. In most of the States, and in the Federal courts, trover lies for the conversion

Fisher v. Essex Bank, 5 Gray, 373, 377 (1855); People's Bank v. Kurtz, 99 Penn. St. 344, 349 (1882); Humble v. Mitchell, 11 Adol. & El. 205, 208 (1839). Cf. Kellogg v. Stockwell, 75 Ill. 68 (1874); *In re* Jackson, L. R., 12 Eq. 354 (1871).

¹ Jermain v. Lake Shore, &c., R. R. Co., 91 N. Y. 483, 492 (1883); Neiler v. Kelley, 69 Penn. St. 403, 407 (1871); Payne v. Elliot, 54 Cal. 339, 341 (1880).

² Pickering v. Appleby, 1 Comyn's Rep. 354 (1721); Humble v. Mitchell, 11 Adol. & El. 205 (1839). But see also, Massell v. Cooke, Finch's Prec. in Chan. 533 (1720).

³ See Chapter XX.

⁴ Nightingal v. Devisme, 5 Burr. 2589; s. c. 2 Wm. Black. 684 (1770); Jones v. Brinley, 1 East, 1 (1800); Douglas v. Congreve, 1 Keen. 410 (1836).

⁵ Ogle v. Knipe, 38 L. J. (Chan.) 692 (1869); Godsen v. Dotterill, 1 Mylne & K. 56 (1832); Lowe v. Thomas, 5 De G., M. & G. 315 (1854); Hotham v. Sutton, 15 Ves. 320 (1808); Atkins v. Gamble, 42 Cal. 86 (1871); Wilson v. Little, 2 N. Y. 443 (1849); Mechanics' Bank v. New York, &c., R. R. Co., 13 N. Y. 599, 626 (1856).

⁶ New Orleans National Banking Association v. Wiltz, 10 Fed. Rep. 330 (1881); s. c. 4 Woods, 43. See also Smith v. Crescent City, &c., Slaughterhouse Co., 30 La. Ann. 1378 (1878).

⁷ See Chapter on Non-negotiability of Stock, and Part II in general.

⁸ See Chapter on Attachment and Execution.

⁹ See Chapter on Taxation.

of stock. In Pennsylvania, however, a contrary rule prevails, although conversion is held to lie for the conversion of certificates of stock.¹

§ 8. *Law of place governing stock.*—Justice Story, in his *Conflict of Laws*, says that questions relating to shares of stock are to be determined by the law of the State of the corporation.² For purposes of attachment and execution levied upon stock this is undoubtedly true, since it is only at the domicile of the corporation that such an attachment or execution can be levied.³ As regards the taxation of stock, however, the stock follows the domicile of the stockholder, and may be taxed in accordance with the law of the domicile of such stockholder.⁴ In reference to transfers of stock, greater difficulty appears. The authorities seem to hold that the transfer must be made in accordance with the law of the State of the corporation, and so far as legal proceedings against the stock, at the domicile of the corporation, are concerned, this is the rule.⁵ A different rule seems to prevail as regards the method of transfer of stock by a married woman, and it is held that a transfer made in accordance with the law of her domicile is valid and effectual, without reference to the law governing married women's rights in the State where the corporation exists.⁶

As regards the common law and statutory liability of a stockholder on his stock, the law of the domicile of the corporation determines the extent of the liability, while the law of the *forum* determines the method of enforcing that liability.⁷

§ 9. *Classes of stock.*—The capital stock of a corporation

¹ See Chapter on Conversion and Measure of Damages.

² Story on Conflict of Laws, 8th ed. § 383.

³ See Chapter on Attachment and Execution.

⁴ See Chapter on Taxation of Stock; Delaware Railroad Tax, 18 Wall. 206, 230 (1873).

⁵ See *Noyes v. Spaulding*, 27 Vt. 420 (1853); *Richmondville Mfg. Co. v. Prall*, 9 Conn. 487 (1833); *Black v. Zacharie*, 3 How. 483 (1845). As regards national banks, see *Scott v. Pequonnock Natl. Bk.*, 15 Fed. Rep. 494 (1883); *Continental Natl. Bk. v. Eliot Natl. Bk.*, 12 Rep. 35; *Dickinson v. Central Natl. Bank*, 129 Mass. 279; *Sibley v. Quinsigamund Natl.*

Bk., 133 Mass. 515 (1882). *Of. State v. First Natl. Bk. &c.*, 89 Ind. 302 (1883). The case of *Glenn v. Clabaugh*, 3 Atl. Rep. 902 (1886), holds that the insolvent laws of Maryland cannot discharge a Maryland subscriber to a Virginia corporation. The validity of a contract to sell stock under the Statute of Frauds is determined by the *lex loci contractus*. *Tisdale v. Harris*, 20 Pick. 9.

⁶ See *Hill v. Pine River Bk.*, 45 N. H. 300 (1864); *Dow v. Gould &c.*, S. M. Co., 31 Cal. 629 (1867). See also *Ross v. Southwestern R. R. Co.*, 53 Ga. 514.

⁷ *New Haven, &c., Co. v. Linden Spring Co.* (Mass., 1886), 6 Eastern Rep. 663. See also Ch. XI, XII.

may be either common or preferred. By *common stock* is meant that stock which entitles the owners of it to an equal *pro rata* division of profits, if any there be; one shareholder or class of shareholders having no advantage, priority, or preference over any other shareholder or class of shareholders in the division. By *preferred stock*, or as it is denominated in England, preference shares, is meant stock which entitles its owners to dividends out of the net profits before or in preference to the holders of the common stock. Common stock entitles the owner to a *pro rata* of dividends equally with all other holders of the stock; while preferred stock entitles the owner to a priority in dividends or earnings.

By *watered or fictitious stock* is meant stock which is issued as fully paid up, when, in fact, the whole amount of the par value thereof has not been paid in. If any amount less than the whole face value of the stock has not been paid, then the stock is watered to the extent of the deficit. Watered stock is, accordingly, stock which does not represent, in good faith, money paid in to the treasury of the company, or money's worth actually contributed to the working capital of the concern. The issue of such stock may be lawful, but it is generally in fraud of the rights of some interested party, as, *e. g.*, creditors of the corporation, certain shareholders or classes of shareholders, or of the public.¹

By *deferred stock* is meant stock the payment of dividends upon which is expressly postponed until some other class of shareholders are paid a dividend, or until some certain obligation or liability of the corporation is satisfied.

By *overissued or spurious stock* is meant stock issued in excess of the full amount of capital stock authorized by the charter of the corporation. Such stock may be issued in good faith, but usually is uttered with a fraudulent intent.

In Massachusetts some classes of corporations issue what is there known as *special stock*. This is a peculiar kind of stock, essentially local in character, provided for by statute, and unknown before the year 1855. Its characteristics are that it is limited in amount to two-fifths of the actual capital; it is subject to redemption by the corporation at par after a fixed time, to be specified in the certificate; the corporation is bound to pay a

¹ See Chapter III, on Issue of Fictitiously Paid-up Stock.

fixed half-yearly sum or dividend upon it as a debt; the holders of it are in no event liable for the debts of the corporation beyond the amount of their stock, and the issue of special stock makes all the general stockholders liable for all debts and contracts of the corporation until the special stock is fully redeemed.¹

§ 10. *Certificates of stock.*—A certificate of stock is from one point of view a mere muniment of title, like a title deed. It is not the stock itself, but evidence or warrant of the ownership of the stock, that is to say, it is a written acknowledgment by the corporation of the interest of the shareowner in the corporate property and franchises; it operates to transfer nothing from the corporation to the shareholder, but merely affords to the latter evidence of his rights. It should be clearly apprehended that the certificate is not the stock, but merely written evidence of the ownership of shares.² Accordingly, it is said that shares have no “earmarks”—that one share cannot be distinguished from another share—but that it is only the certificates which are distinguishable one from the other by their numbers and in other ways.³ The certificate, therefore, has value in itself only as evidence, and apart from the shares which it represents it is utterly worthless.⁴ And even as evidence it is not in every case essential; it is merely a convenient voucher, which the shareholder has a right to receive if he asks for it.⁵ One element of its value to the shareholder is that it is *prima facie* evidence of his title.⁶

¹ American Tube Works v. Boston Machine Co., 139 Mass. 5 (1885); Williams v. Parker, 136 Id. 204, 207 (1884); Reed v. Boston Machine Co., Sup. Jud. Ct. of Mass. (1886); Stats. of Mass. 1855, chap. 290; 1870, chap. 224, §§ 25, 39, cl. 4; Pub. Stat. of Mass., chap. 106, §§ 42, 61, cl. 3.

² Hawley v. Brumagim, 33 Cal. 394 (1867); Campbell v. Morgan, 4 Bradw. 100 (1879); People's Bank v. Kurtz, 99 Penn. St. 344 (1882); Hubbell v. Drexel, 21 Am. Law Reg. (N. S.) 452 (1881); Van Allen v. Assessors, 3 Wall. 573, 598 (1865); Burr v. Wilcox, 22 N. Y. 551 (1860). “Stock is one thing, and certificates another. The former is the substance, and the latter is the evidence of it.” Hawley v. Brumagim, *supra*.

³ Hubbell v. Drexel, *supra*.

⁴ Payne v. Elliot, 54 Cal. 339.

⁵ Johnson v. Albany, &c., R. R. Co., 40 How. Prac. 193 (1870). Cf. Arnold v. Suffolk Bank, 27 Barb. 424 (1857), a

case in which the distinction between a refusal on the part of a corporation to issue a certificate in a certain form, and a refusal to recognize the owner of shares as owner—a denial of his property in the stock—is clearly drawn. By the Supreme Court of Indiana the distinction to the effect that a certificate is not the title, but only evidence of the title, to shares is clearly drawn. The court says: “The certificate did not constitute the title to the stock. The registry of the stockholder's name upon the stock books of the company, opposite the number of his shares, gave him his title. In legal contemplation the certificate was merely an additional and convenient evidence of the ownership of the stock.” Cincinnati, &c. R. R. Co. v. Pearce, 28 Ind. 502 (1867).

⁶ Broadway Bank v. McElrath, 13 N. J. Eq. 24 (1860); Courtright v. Deeds, 37 Iowa, 503 (1873); Walker v. Detroit Transit, &c. Co., 47 Mich. 338 (1882).

The right of every shareholder to demand and receive from the company a certificate is generally conceded.¹ When certificates are executed by a part only of the officers required by law to sign them, they are void.² But a certificate issued to an officer of the corporation who is a shareholder, although the certificate is signed by that officer, is valid.³ It is not, however, essential to the existence of the corporation, that certificates of stock shall be issued.⁴ Without a certificate the shareholder has a complete power to transfer his stock,⁵ to receive dividends,⁶ and to vote,⁷ and he is individually liable as a stockholder.⁸ A certificate of stock may be a valid subject of a *donatio causa mortis*, of a legacy, a contract of sale, a pledge, or a gift.⁹ Under the English statute an issue of stock by a corporation has reference only to the issue of the certificates, and means an original putting out of the shares.¹⁰ In New York, making out and mailing the certificates has been held to constitute a due issuing thereof.¹¹ And in Maryland, the stub of a book from which certificates have been detached is evidence of their regular issue.¹²

¹ *Buffalo, &c. R. R. Co. v. Dudley*, 14 N. Y. 336, 347 (1856); *National Bank v. Watsontown Bank*, 105 U. S. 217 (1881); *Chester Glass Co. v. Dewey*, 16 Mass. 94 (1819). A valid certificate may be issued out of the State in which the corporation exists. *Courtright v. Deeds*, 37 Iowa, 503 (1873).

² *Holbrook v. Farquier, &c. Co.*, 3 Cranch C. C. 425 (1829).

³ *Titus v. President, &c. of the G. W. Turnpike Road*, 61 N. Y. 237 (1874).

⁴ *Chester Glass Co. v. Dewey*, 16 Mass. 94 (1819); *Burr v. Wilcox*, 22 N. Y. 551 (1860).

⁵ *First National Bank v. Gifford*, 47 Iowa, 575 (1877); *National Bank v. Wat-*

sontown Bank, 105 U. S. 217 (1881). *Cf. Brigham v. Mead*, 10 Allen, 245 (1865).

⁶ *Ellis v. Proprietors of Essex Merri-mack Bridge*, 2 Pick. 243 (1824).

⁷ *Beckett v. Houston*, 32 Ind. 393 (1869).

⁸ *Agricultural Bank v. Wilson*, 24 Me. 273 (1844); *Mitchell v. Beckman*, 64 Cal. 117 (1883).

⁹ See Chapter XVIII, on Legacies and Gift of Stock.

¹⁰ *East Gloucestershire Ry. Co. v. Bartholomew*, L. R. 3 Exch. 15 (1867); *Bush's Case*, L. R. 9 Chan. 554 (1874).

¹¹ *Jones v. Terre Haute, &c. R. R. Co.*, 17 How. Pr. 529 (1859).

¹² *Weber v. Fickey*, 47 Md. 196 (1877).

CHAPTER II.

METHODS OF ISSUING STOCK.

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not as a contract right. |
| 12. First method.—Issue by money
subscription. | 17. Sale of stock for property. |
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| 15. What property may be received. | 20. Third method.—Issue by stock
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§ 11. *Methods of issuing stock.*—There are in general three methods of issuing stock. It may be issued, first, by means of subscriptions, payable in cash, the subscription being made in writing or by acts equivalent thereto.¹ Second, the issue may be by means of subscriptions, payable by its terms, in labor, property, or both, or by means of a sale of stock for labor, property, or both. Third, the issue may be by a stock dividend.

§ 12. *First method.—Issue by money subscription.*—An issue of stock by means of a subscription, payable in cash, is the most usual, honest, and satisfactory method of issuing stock. In the absence of any agreement to the contrary, an ordinary subscription for stock is deemed a cash subscription, and payment in money may be enforced.² The subscription contract is generally made by a writing duly signed by the subscriber. The writing itself is contained in books opened by the corporation or by commissioners appointed in conformity with a statute, or it is made without formality, on subscription lists or separate sheets of paper.

A subscription, payable in cash, may arise also from the mere acts or declarations of a party. A person having assumed the position of a subscriber or stockholder is frequently held to be bound as such. Any act or declaration, sufficient to indicate an intent on the part of the person to be a subscriber, and an accept-

¹ See Chapter IV.

² See Chapter IX.

ance, by the corporation, of the person as such, is equivalent to a written subscription, and the person is barred as a subscriber.¹

§ 13. *Second method.—Issue for property, labor, or to a construction company.*—The issue of stock for labor, property, contract work, or any valuable consideration other than money, has given rise to much controversy and litigation. In England a long line of decisions, under the Companies Acts, has established the principle that stock need not necessarily be paid for in cash, but that it may be paid for in money's worth.² Such also was the rule at common law.³ The well-established rule now is that a subscription for stock, payable by its terms in property or labor, or both, is a good and legal subscription. If the property is taken at a valuation made without fraud, the payment is as effectual and valid as though made in cash to the same amount. An issue of stock for property is one which finds support, not only in the decisions, but in the daily transactions of corporations,⁴ and the law does not compel the corporation and the subscriber to go through the useless form of a payment by the corporation to the subscriber of the value of the property, and an immediate repayment of the same money by the subscriber to the corporation on his subscription.⁵

¹ See Chapter IV.

² See many cases in Chapter III. *Stacy v. Little Rock & Fort Smith R. R. Co.*, 5 Dill. 348, 376 (1879).

³ *Woodhall's Case*, 3 De G. & Sm. 63 (1849), and in *Burkinshaw v. Nichols L. R.*, 3 App. Cas. 1004, 1012 (1878), payment having been made in property, the court said: "If there had been no statutory enactment forbidding a transaction of that kind, it is a transaction which might be properly valid." *Cf. dictum* in *Sanger v. Upton*, 91 U. S. 56, 60 (1875). "It is not now questioned that a corporation may issue its stock by way of payment in the purchase of property. This is on the principle that there is no need for the roundabout process of first issuing the stock for money, and then paying the money for the property. But it is necessary that the property so taken be considered reasonably worth the par value of the stock paid for it." *Chouteau v. Dean*, 7 Mo. App. 210 (1879); *Wyman v. Amer. Powder Co.*, 62 Mass. 168 (1851); *Reichwald v. Commercial Hotel Co.*, 106 Ill. 439 (1883); *Haydon v. Atlanta Cotton Factory*, 61 Ga. 234 (1878).

⁴ *Foreman v. Bigelow*, 4 Cliff. 508, 544 (1878).

⁵ *Seawright v. Payne*, 6 Lea (Tenn.), 283 (1880); *Brant v. Ehlen*, 59 Md. 1 (1882); *Spargo's Case*, L. R. 8 Ch. App. 412 (1873); *Boot & Shoe Co. v. Hart*, 56 N. H. 548 (1876). Payment in property by subscribers was held not allowable in *Neuse River Nav. Co. v. Com'rs of Newbern*, 7 Jones' Law (N. C.) 275 (1859); also *Henry v. Vermillion & Ashland R. R. Co.*, 17 O. 187 (1843), although the latter case seems to involve an oral agreement to allow such payment, and to have been decided on that ground. *Greenhood on Public Policy*, 136 (1886), improperly applies hereto the rule relative to special agreements with part of persons jointly interested in an enterprise. There is a long line of cases sustaining the validity of an issue of stock for money's worth instead of money itself. They are given in this and the following chapter. So well established has this principle of law become that the few cases holding to the contrary can no longer be considered good law. "That in the absence of fraud an agreement

There is some doubt as to whether an oral agreement of the corporate agents, that a subscription may be paid in property is binding upon the corporation. Under the well-established rule that parol evidence will not be allowed to add to or vary a written agreement, it has been held that such an oral agreement with the agent cannot be admitted in evidence.¹ When, however, the parol agreement is made subsequently to the act of subscribing, and is supported by a sufficient consideration, it is valid and enforceable.²

§ 14. *When such subscriptions are not legal.*—A subscription payable by its terms in labor or property is in the nature of a conditional subscription. Accordingly, in certain States, where a percentage or fixed amount of the capital stock must be subscribed for before a charter can be obtained; and where, by the decisions of the courts, such preliminary subscriptions must be absolute and unconditional; a subscription payable by its terms in labor or property, being conditional to that extent, cannot form a part of the preliminary subscription.³ In such States, however, subscriptions to the remainder of the capital stock, the part not subscribed for, in order to obtain the charter, may be conditional, and may, by their terms, be payable in property or labor.⁴ On the ground that subscriptions payable

may ordinarily be made by which stockholders could be allowed to pay for their shares in patents, mines, or other property, to which it is not easy to assign a determinate value, would appear to be well settled." *New Haven, &c., Co. v. Linden Spring Co.*, 6 Eastern Rep., 663 (Mass. 1886). Frequently statutes are passed regulating the issue of stock for property. In New York, by statute, ten per cent. of preliminary subscriptions to railroad corporations must be paid in cash, but the remaining ninety per cent. may be issued for property. Manufacturing corporations in New York may now issue stock for property. § 14 of Laws of 1848, ch. 40, was amended by Laws 1853, ch. 333, so as to allow such payments. In Building Corporations payment for stock can be in money only. Laws 1853, ch. 117, § 14. See *People v. Troy House Co.*, 44 Barb. 625.

¹ Thus a parol agreement that part payment in contract labor should be allowed was held to be void, inasmuch as it varied the terms of a written agreement.

Ridgefield & N. Y. R. R. Co. v. Brush, 43 Conn. 86 (1875). *Contra*, *Louisville & Nash. R. R. Co. v. Thompson*, 18 B. Monr. 735 (1857); *McConahy v. Centre & Kish Turnpike R. Co.*, 1 Penn. & W. 426 (1830), followed in *Swatara R. R. v. Brune*, 6 Gill, 41 (1847); overruled by *Nippenose Mfg. Co. v. Stadon*, 68 Pa. St. 256 (1871). See also *Weber v. Fickey*, 52 Md. 501; *Leibke v. Knapp*, 79 Mo. 22 (1883). On this subject see also Chapter IX.

² *Pittsburgh & Connellsville R. R. Co. v. Stewart*, 41 Pa. St., 54 (1861).

³ *Erie & Waterford Plank Road Co. v. Brown*, 25 Pa. St. 156 (1855); *Nippenose Mfg. Co. v. Stadon*, 68 Pa. St. 256 (1871); *Pittsburgh & Connellsville R. R. Co. v. Stewart*, 41 Pa. St. 54 (1861). But after the corporation has obtained its letters patent and completed its organization it may receive subscriptions, payable by their terms in property. *Phil. & West Chester R. R. Co. v. Hickman*, 28 Pa. St. 318 (1857.) See Chapter on Conditional Subscriptions.

⁴ See *Id.*; also *Dayton & Cincinnati*

in property or labor are conditional, it has been held also that a subscription payable in labor or property is not to be counted in ascertaining whether the full capital stock has been subscribed,¹ but it is doubtful whether such a rule can be considered good law.

§ 15. *What property may be received.*—A corporation may receive in payment of its shares of stock any property which it may lawfully purchase,² and, in general, may receive any consideration which is suitable and applicable to the purposes for which the corporation was organized.³ A railroad corporation may receive payment in contract work, in right of way, or in any kind of material or labor applicable to its construction.⁴ A manufac-

R. R. Co. v. Hatch, 1 Disney, 84 (1855); § 17 n.

¹ If it is counted, an action against another subscriber on his subscription may be defeated thereby. New York, Housatonic & Northern R. R. Co. v. Hunt, 39 Conn. 75 (1872); Cabot & West Springfield Bridge v. Chapin, 60 Mass. 50 (1850); *contra* Phillips v. Covington & Cincinnati Bridge Co., 2 Metc. (Ky.) 219 (1859). See also Chapter on Conditional Subscription.

² Brant v. Ehlen, 59 Md. 1 (1882); The American Silk Works v. Saloman, 4 Hun, 135 (1875).

³ See Green's Brice's Ultra Vires (3d ed.), 145; Angell & Ames (11th ed.), § 517. "Payment of stock subscriptions need not be in cash, but may be in whatever, considering the situation of the corporation, represents to that corporation a fair, just, lawful, and needed equivalent for the money subscribed." Liebke v. Knapp, 79 Mo. 22 (1883). Payment in newspaper advertising of the enterprise upheld in this case. The subscription may by its terms be payable in plank for a plank road company, and the subscriber is a stockholder before payment is completed. Haywood & Pittsboro' Plank Road Co. v. Bryan, 6 Jones' Law (N. C.), 82 (1858). Payment in Confederate bonds redeemable in cotton upheld. Schroder's Case, L. R. 11 Eq. Cas. 131 (1870). So, also, payment in stock in a coal corporation carrying on a supplementary business. East N. Y. & Jamaica R. R. Co. v. Lighthouse, 4 Rob. (N. Y.) 407. Payment by a patent right has been upheld. Edwards v. Bringier Sugar Extracting Co., 27 La. Ann. 118 (1875); and in another case, under a statute not upheld. Tasker v.

Wallace, 6 Daly, 364 (1876). Payment may be by cancelling a debt of the company past due. Carr v. Le Fevre, 27 Pa. St. 413 (1856); Reed v. Hayt, 51 N. Y. Super. Ct. 121 (1884). Or not yet due. Appleyard's Case, 49 L. J. (Ch.) 290 (1880). Payment, however, to a bank in its own currency was not upheld, it being held that only specie could be received. King v. Elliott, 13 Miss. 428 (1845). Payment by check cannot be objected to by another subscriber. Thorp v. Woodhull, 1 Sandf. Ch. 411 (1844).

⁴ "We can see no objection whatever to a railroad company issuing stock and taking in payment materials or labor or land necessary for its road." Clark v. Farrington, 11 Wis. 306 (1860). "The corporation had a right to accept payment of stock in labor or materials, in damages which the company were liable to pay, or in any other liability of the company, provided these transactions were entered into and carried out in good faith." Phil. & West Chester R. R. Co. v. Hickman, 28 Pa. St. 318 (1857); Bedford County v. Nashville, C. & St. Louis R. R. Co., 14 Lea (Tenn.), 525 (1884), holding, also, that thirty years' delay in demanding the stock is no bar to the right. Payment may be in cross ties. Ohio, Ind. & Ill. R. R. Co. v. Cramer, 23 Ind. 490 (1864). Or in real estate and services. Cin. Ind. & Chicago R. R. Co. v. Clarkson, 7 Ind. 595 (1856). Or in services and materials. Phillips v. Covington & Cin. Bridge Co., 2 Metc. (Ky.) 219 (1859). Or by the construction of the road. See § 17. One railroad having power to consolidate with another may, in payment therefor, issue stock to the contractors who are constructing the lat-

turing corporation may receive payment in the good will of a business or the stock in trade.¹ Land may be taken in payment when the corporation would be allowed to purchase the same.² Promissory notes may also be taken, under the corporate power, to give credit and extend the time of payment of debts.³

§ 16. *Payment in property as a favor, not as a contract right.*—There is an important distinction to be made between payments in property, where the subscription itself, by its terms, allows such payment, and a payment in property which is allowed, as a matter of favor, by the corporation, the subscription itself being silent as to the mode of payment.⁴ The latter class of trans-

ter. *Branch v. Jesup*, 106 U. S. 468 (1882).

¹ *Pell's Case*, L. R. 5 Ch. 11 (1869).

² *Goodin v. Evans*, 18 O. St. 150 (1868); *Cin. Ind. & Chicago R. R. Co. v. Clarkson*, 7 Ind. 595 (1856); *Peck v. Coalfield Coal Co.*, 11 Bradw. (Ill.) 88 (1882); *Brant v. Ehlen*, 59 Md. 1 (1882); *Jones' Case*, L. R. 6 Ch. App. 48 (1870); *Maynard's Case*, 22 W. R. 119. In *Foreman v. Bigelow*, 4 Cliff. 508, 544 (1878), the court says: "Argument to show that the transaction of issuing the stock in payment for the mineral land would have been valid . . . is scarcely necessary." In Indiana formal acceptance by the directors is necessary. *State v. Bailey*, 16 Ind. 46 (1861); *Junction R. R. Co. v. Reeve*, 15 Ind. 236 (1861); *Dayton, &c. R. R. Co. v. Hatch*, 1 Disney, 84 (1855); *Carr v. Le Fevre*, 27 Penn. St. 418 (1856); *Johnson v. N. Y. & Erie R. R. Co.*, 2 Sand. 39 (1848).

³ *Stoddard v. Shetucket Foundry Co.*, 34 Conn. 542 (1868); *Ogdensburgh, &c. R. R. Co. v. Wooley*, 3 Abb. Ct. of App. Dec. 398 (1864); *Magee v. Badger*, 30 Barb. 246 (1859); *Goodrich v. Reynolds*, 31 Ill. 490 (1863); *Vermont Central R. R. Co. v. Claves*, 21 Vt. 30; *Hardy v. Merriweather*, 14 Ind. 203. In Wisconsin a corporation may accept in payment of stock a note secured by a mortgage on real estate. *Clark v. Farrington*, 11 Wis. 306 (1860); *Blunt v. Walker*, 11 Wis. 234 (1860); *Cornell v. Hichens*, 11 Wis. 353 (1860); *Lyon v. Ewings*, 17 Id. 61 (1863); *Andrews v. Hart*, Id. 297; *Western Bk. of Scotland v. Tallman*, 17 Wis. 530 (1863). In Tennessee payment in notes is not upheld, but the subscriber is to be credited with the amount collected on such notes. *Moses v. Ocoee Bank*, 1 Lea (Tenn.), 398

(1878). In New York the payment of a subscription by one's own note is prohibited by statute. 1 R. S. Chap. 18, Title 4, § 2. Payment by bond and mortgage was upheld in *Valk v. Crandall*, 1 Sandf. Ch. 179 (1843); and in *Leavett v. Pell*, 27 Barb. 322 (1858). In Pennsylvania—see *Leighty v. Susquehanna & Waterford T. Co.*, 14 S. & R. 434 (1826)—the payment being contrary to statute; also, *People v. Stockton, &c. R. R. Co.*, 45 Cal. 306 (1873).

⁴ Many of the cases which apparently are cases of subscriptions wherein the subscriber has expressly stipulated that he may pay in property or labor, will be found, on close examination, to be absolute subscriptions payable in cash. Afterwards the corporation, although not obliged so to do, accepts property or labor instead of the cash. This kind of transaction is almost universally upheld by the courts, when entered into and carried out in good faith. Such payment is upheld even in opposition to the express terms of a statute requiring payment in cash. See § 18. Many of the American cases, also, are plainly cases in which payment in property was allowed by the corporation, not as a right but as a matter of favor. The courts upheld such agreements because they are similar to offsets of accounts, and the delays, uncertainties, special privileges, and other objections to subscriptions payable in terms in property and labor are obviated. See *Boot & Shoe Co. v. Hoit*, 56 N. H. 548 (1876); *Stoddard v. Shetucket Foundry Co.* 34 Conn. 542 (1868), where the court says, "that the defendant could have insisted upon the plaintiff's payment for his stock in cash is unquestionable." See also *Vermont Central R. R. Co. v.*

actions have been uniformly upheld, except when positively prohibited by statute. Such payment has been held to be valid, although the statute required payment to be in money or in cash.

§ 17. *Sale of stock for property.*—The issue of stock for property, labor, or contract work need not necessarily be accompanied with the formality of a subscription.¹ Frequently the issue is in the form of a sale of the stock for the property received in payment. Such a transaction is not a sale, however, since the stock has a fixed value, the par value, which, in the original issue, must be considered its market value.² Sometimes the issue is by means of a contract, whereby, upon the completion of certain work, the party is to be entitled to the stock. The New York Court of Appeals stated the law clearly when it said, in respect to such issues, that “the right of the officers of a railroad corporation to enter into an agreement to build its road and pay for the construction of the same in stock or bonds cannot be seriously questioned, and contracts of this description are frequently made for such a purpose.”³ It is doubtful, however, whether any clear-

Clayes, 21 Vt. 30 (1848); *Boston, &c., R. Co. v. Wellington*, 113 Mass. 79 (1873). In New York, railroad corporations must require payment in cash of a certain percentage of the subscription at the time of subscribing. Laws 1850, ch. 140, §§ 2, 4. Ninety per cent. may be paid in such manner as the directors may require. Id. § 7. Even here, however, the courts hold that the ten per cent. may be paid by property actually received. *Beach v. Smith*, 30 N. Y. 116 (1864), where payment was by services rendered. The court said: “Was it necessary for any purpose that the ceremony of paying money by the company to the defendant and by the defendant of the same money back again, should be gone through with? It seem to me not.”

¹ A charter provision authorizing the opening of stock subscription books, does not amount to a prohibition against any other mode of becoming a stockholder. “If a railroad could sell its stock for the right of way, for lands for depot purposes, for iron or anything essential to the accomplishment of its purpose, it might do so.” It is a legal issue of stock without subscription. *Western Bk. of Scotland v. Tallman*, 17 Wis. 530 (1863). See also *Clark v. Farrington*, 11 Wis. 306 (1860);

Reed v. Hayt, 51 N. Y. Super. Ct. 121 (1884). In *Jackson v. Traer*, 20 Northw. Rep. 764 (Iowa, 1884), stock having been issued in payment of contract work, the court says: “We have seen no case which recognizes a difference between those stockholders who become such in pursuance of a written agreement, and those who become such by the mere acceptance of stock issued to them.”

² See Chap. III on this subject.

³ *Van Cott v. Van Brunt*, 82 N. Y. 535 (1880). See also *Eppes v. Miss., Gainesville & Tuscaloosa R. R. Co.* 35 Ala. 33 (1859), *Brady v. Rutland & Burlington R. R. Co.* 3 Blatchf. 25; s. c. 24 Vt. 660; *Troy & Greenfield R. R. Co. v. Newton*, 8 Gray, 596 (1857). If the corporation prevents the completion of the contract, the contractor may recover, as damages, the value of work already done, and also the profits lost. *Myers v. York & Cumberland R. R. Co.* 2 Curtis, 28 (1854). If the corporation refuse to issue the stock, according to contract, the contractor may recover as damages the market value of the stock. *Porter v. Buckfield Branch R. R.* 32 Me. 539 (1851); *Barker v. Rutland & Washington R. R. Co.* 27 Vt. 766 (1855). If the contract provides for payment to the contractor, in stock, with-

ness of ideas is obtained, under any circumstances, by calling an original issue of stock a sale of stock. A sale of stock means a transfer of stock after the stock has been issued, or an agreement to transfer the same. Such original issues of stock, as are occasionally spoken of as being sales of stock, might better be considered as informal subscriptions arising by the acts or declarations of the parties, and payable in property by the terms of a contract.¹

§ 18. *English statutes on issues of stock for property.*—In England the payment for stock in property, labor, or contract work is regulated largely by Act of Parliament. The statute requires that payment shall be in cash, unless the contract allowing payment in property is registered at a specified public registry.² Nevertheless the courts have held that a payment in property is equivalent to a payment in cash, where the property has been actually delivered, and such payment will be upheld.³ Such a payment in property, however, is as a matter of favor, and not of right.⁴ It is to be distinguished from the payment in property which the subscriber may not yet have made, but has a right to

out stating that the stock is to be taken at its par value, the contractor may demand the stock at its market value, and if it is worthless, he may then demand money in lieu thereof. *Hart v. Lauman*, 29 Barb. 410. The contractor cannot, however, complain because the capital stock has been increased, nor is a tender of the stock to him necessary. *Moore v. Hudson River R. R. Co.*, 12 Barb. 156 (1851).

¹ See *Weiss v. Mauch Chunk Iron Co.*, 58 Penn. St. 295 (1868); *St. Paul, &c., R. R. Co. v. Robbins*, 23 Minn. 440 (1877); *Clark v. Continental Improvement Co.*, 57 Ind. 135 (1877).

² Companies Act, Amendment 1867, 30 and 31 Vic. ch. 131, § 25.

³ Under this statute, three classes of cases of unregistered contracts arise. First, where payment is actually made in property, if fairly made, it is upheld, under the principles laid down in § 16. See *Jones' Case*, L. R. 6 Ch. App. 48 (1870); *Maynard's Case*, 22 W. R., 119 (1873); payment by colliery, *Re Boylan Hull Colliery Co.*, L. R. 5 Ch. App. 346 (1870); *Drummond's Case*, L. R. 4 Ch. App. 772 (1869); *Schroder's Case*, L. R. 11 Eq. Cas. 131 (1870); *Pell's Case*, L. R. 5 Ch. 11 (1869); by services, *Ex parte Clarke*, L. R. 7 Eq. 550. The amounts on each side

must be payable presently and in cash. *Fothergill's Case*, L. R. 8 Ch. App. 270 (1873); so that the transaction is in the nature of a setoff; *Forbes' Case*, L. R. 5 Ch. App. 270 (1870). Conveyance of a lease held to be a good payment. *Spargo's Case*, L. R. 8 Ch. App. 407 (1873). A second class of unregistered agreements to take pay in property, turn upon the question whether the condition to the subscription is precedent or subsequent. If the condition is precedent, and must be performed before the subscription can be enforced, none of the parties are bound, even though the corporation becomes insolvent. *Pellatt's Case*, L. R. 2 Ch. 527 (1867); *Stace's Case*, L. R. 4 Ch. App. 682 (1869). The third class is where the contract to pay in property is construed to be a condition subsequent. The condition being subsequent, the party must pay; and if the corporation becomes insolvent, he must pay in cash. *Elkington's Case*, L. R. 2 Ch. App. 527 (1867); *Simpson's Case*, L. R. 4 Ch. App. 184 (1868); *Bridger's Case*, L. R. 5 Ch. App. 305 (1870); *Thomson's Case*, 34 L. J. (Ch.) 525 (1865); *Fisher's Case*, 53 L. Times Rep. 832 (1886); *Sherrington's Case*, 34 Weekly Rep. 49 (1885). See also Chap. III, § 35.

⁴ See § 16.

make in the future. The one is an executed contract. The other may still be an executory contract.

§ 19. *Performance of contract of payment in property.*—Subscriptions payable in property are not subject to calls, and a demand for the property must be made by the corporation.¹ Upon failure of the subscriber to furnish the property, or upon insolvency of the corporation, such subscriptions become payable in cash.² A payment of part of the subscription in cash does not waive the right of the subscriber to pay the balance in property.³

§ 20. *Third method of issue, by stock dividend.*—The third method of issuing stock is by a stock dividend. It is allowable when an amount of cash or property equal to the amount of the par value of the stock so divided is added permanently to the capital stock of the corporation. A cash dividend can be made only when the whole of the capital stock has not been issued, or when it may be increased. It can never increase the capital stock beyond the amount as limited by legislative enactment. An issue of stock by a stock dividend is prohibited by constitutional or legislative enactment in some States. In England it has been a question of doubt whether stockholders can be compelled to accept a dividend of stock. These questions, however, are discussed elsewhere.⁴

¹ Ohio, &c., R. R. Co. v. Cramer, 23 Ind. 490 (1864). Payment cannot be required in installments. Id. But upon demand, the subscriber must ascertain when and where the materials are to be delivered. McClure v. People's R. R. Co. 90 Pa. St. 269 (1879).

² Haywood, &c., R. R. Co. v. Bryan, 6 Jones (N. C.), 82 (1858); Sperry v. Johnson, 11 O. 452 (1842). See § 18, n. 3.

In one case, however, it was held that the subscriber was liable only in damages to the extent of the market value of the stock. Dayton & Cin. R. R. Co. v. Hatch, 1 Disney, 84 (1855).

³ Pittsburgh, &c., R. R. Co. v. Stewart, 41 Pa. St. 54 (1861).

⁴ See Chapter on Paid-up Stock and Chapter on Dividends.

CHAPTER III.

THE ISSUE OF FICTITIOUSLY PAID UP STOCK.

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| <p>§ 21. Objects of such issues.</p> <p>22. Methods of issue.</p> <p>23. Unsatisfactory <i>dicta</i> of the courts as to their legality.</p> <p>24. The important questions involved herein.</p> <p>25. Fictitious stock not void.</p> <p>26. Constitutional provisions making it void.</p> <p>27. Statutes making it void.</p> <p>28. English statutes.</p> <p>29. Fictitious stock may be voidable.</p> <p>30. Issue by first method.—At a discount in cash.</p> <p>31. Dangers of this method.</p> <p>32. English rule under statute.—Sustains issues below par.</p> <p>33. Second method.—Issue for property at an overvaluation.</p> | <p>§ 34. New York rule.</p> <p>35. English statute and rule.</p> <p>36. Dangers of this method.</p> <p>37. Who may complain.—The State.</p> <p>38. — The corporation.</p> <p>39. — Stockholders participating.</p> <p>40. — Transferees of participating stockholders.</p> <p>41. — Dissenting stockholders.</p> <p>42-44. — Corporate creditors.</p> <p>45. Who is liable.—The corporation.</p> <p>46-47. — Person receiving the stock.</p> <p>48. — Officers of the corporation.</p> <p>49. — Transferees with notice.</p> <p>50. — <i>Bona fide</i> transferees.</p> <p>51. Third method.—Issue by stock dividend.</p> |
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§ 21. *Objects of issuing fictitiously paid up stock.*—The issue of shares of stock as “paid up,” when, in fact, they are not paid up, gives rise to some of the most complicated questions connected with the law of corporations.

A share of stock is supposed, in theory, to represent its par value in money or money's worth, paid in or to be paid in to the corporation. Accordingly, when it is issued as paid up, it is bought and sold in open market, on the supposition that the corporation has received its full par value. Upon this basis, transactions in paid up stock, involving many millions of dollars, are of daily occurrence in the commercial centres of the country. The facilities which exist for the sale of properly issued stock are equally available for the sale of fictitiously paid up stock, until it has become well understood and expected that railroad and business corporations will make these issues of stock.¹ The

¹ “According to the estimate of the most widely acknowledged statistical authorities upon railways, through the methods of sale or hypothecation, \$3,700,000,000 of purely paper values have been sold to the public.” Hudson on

The Railways and The Republic, 274 (1886), a book that deals with the railway problems of the day, from an anti-railway point of view. See also Preface to Poor's Manual for 1884.

issue is generally to the organizers or their co-operators, in ostensible payment for property or construction work. It is no unusual thing for a newly organized railroad corporation to issue to a construction company, bonds and stock whose par value is many times the value of the construction work done. These bonds and the stock are then sold to the public at a profit, large or small, according to the prospects of the enterprise and the skill of the parties who are manipulating the corporation. Soon, however, default is made in the payment of the interest on the bonds, and this is followed by corporate insolvency, foreclosure, receivership, and reorganization.¹ The issue of fictitiously paid up stock is the favorite device of corporate promoters, organizers, and manipulators, in carrying out their plans of realizing enormous gains from small investments, and in accumulating great fortunes at the expense of the public. Occasionally, too, the issue is made for the purpose of concealing large and unreasonable profits; which, if known, might cause the public to regulate and diminish the source of income. In such cases, a stock dividend is generally resorted to.

§ 22. *Methods of issuing fictitiously paid up stock.*—There are, in general, three different ways in which fictitiously paid up stock may be issued.² It may be by issue of certificates of stock

¹ "Securities in excess of cash investments are produced: (1) by stock dividends of prosperous companies, capitalizing what are called surplus earnings: (2) by issuing the securities of unprosperous roads, for which the companies receive only a portion of their face value: (3) by the purchase of other railways, of mining or manufacturing property, or of real estate, or by consolidation with other companies, paying for the property prices largely in excess of the real value, either in the capital stock of the company or in new securities: and (4) by the construction of railways under contracts by which the projectors, as a railway company, pay to themselves, as contractors, from two to four times the cost of the work in stocks and bonds, selling these to the public as they can." Hudson on The Railways and The Republic, 273.

² Professor Hadley, in his recent work on Railroad Transportation, a work replete with information, argument, and illustration, but, perhaps, with something of a bias towards railway interests, says, p. 55, n. 3: "Stock-watering

has three forms. 1. Where new stock is issued to represent money which, instead of being paid out as a dividend, is used in improving the property. 2. Where new stock is issued to represent an actual increase in the earning capacity and market value of the property, so that the par value shall represent as nearly as possible the real value. 3. Where stock is issued to give certain parties control of the road without actually risking anything like the amount represented by the par value of their shares." This classification can hardly be commended. The first form mentioned is not stock-watering, but is valid and legal as the law now stands. It is a stock dividend, made without fraud and upheld by well established principles of law. See Chapter on Dividends. The third form mentioned by Professor Hadley, is in part a repetition of the second, and merely gives the motive of such issues of stock. The second mode is true stock-watering. But the definition should be made more sweeping, so as to include issues of the original capital stock. All stock whose

for an amount of money less than the par value of the stock, the certificates asserting on their face that the full value has been paid in; or it may be for property or construction work taken at a fraudulent overvaluation; or it may be by a stock dividend, the equivalent par value of which has not been permanently added to the capital stock. Each of these three methods, as was shown in the preceding chapter,¹ may be the means of issuing stock which has been paid up in good faith. Each, also, is available for the issue of fictitiously paid up stock. The second method particularly, that of taking property at an overvaluation, is well calculated to conceal the fictitious character of the issue, and to accomplish the purposes of the participants.

§ 23. *Legality of such issues.*—There are various opinions, generally *dicta*, contained in the cases, as to the character of stock issued as paid up, when, in fact, it has not been paid for. The customary expression is that such an issue is a fraud upon the law and upon the stockholders; or that it is against public policy; or is a fraud on subsequent purchasers of the stock so issued.² Other cases, however, and cases of high authority, hold that an issue of stock as full paid up stock, under an agreement that the full par value shall not be paid, is not necessarily a fraudulent transaction, but that as between the parties thereto, is a legal and valid agreement, and violates no principle of public policy.³

full par value has not been paid in to the corporation, in money or money's worth, is watered to the extent that the par value exceeds the amount so paid in.

¹ See Chapter II.

² In *Barnes v. Brown*, 80 N. Y. 527-534 (1880), the court said in a *dictum*: "It is not claimed, and could not be claimed, that the corporation or its directors could create any valid stock by issuing the same without any consideration. The directors assuming to issue stock in that way would perpetrate a wrong upon the corporation and its stockholders, and a fraud upon every person who took such stock as full paid stock, relying upon the appearances and deceived thereby." In the case of *Sturges v. Stetson*, 1 Biss. 246 (1858), the court said: "The subscription of stock by plaintiff, for less than the price of the shares fixed in the charter, was void, as against law and the power of the directors." See also *Ex parte Daniell*, 1 De Gex & Jones, 372 (1857); *Oliphant v. Woodhaven, &c., Co.*, 63

Iowa, 332 (1884); *Tobey v. Robinson*, 99 Ill. 222, 228 (1881); *Osgood v. King*, 42 Iowa, 478 (1876):

³ In *Scoville v. Thayer*, 105 U. S. 143 (1881), the court says: "It is conceded to have been the contract between him and the company that he should never be called upon to pay any further assessments upon it [the stock]. The same contract was made with all the other shareholders, and the fact was known to all. As between them and the company this was a perfectly valid agreement. It was not forbidden by the charter or by any law or public policy." In the case of *In re Ambrose Lake Tin & Copper Min. Co., L. R.*, 14 Ch. Div. 390, 394-5, where paid up stock was issued for property taken at a gross overvaluation, the court said: "It seems to me impossible to say that, however wrong the transaction was in respect to other persons, there was anything wrong as between the company and the vendors." In *Flinn v. Bagley*, 7 Fed. Rep. 785 (1881), the court held that

§ 24. *The important questions involved.*—These statements of the law, however, throw little light upon the important questions of the dangers, and rights, and liabilities growing out of such issues of stock. The stockholder and the practitioner wish to know whether such stock is void, or is voidable, or is valid. If voidable, it is important to know what are the rights and remedies of the various parties involved. If the stock is valid, then the question arises, whether any one is liable for that part of the par value which has not been paid, and also who may bring suit to enforce that liability.

§ 25. *Fictitious stock is not void.*—Is stock void when fictitiously issued as paid up? It is settled that it is not, and it may be stated as a well established rule, that stock issued as paid up, when it has not been fully and fairly paid up, is not absolutely void, unless it is declared to be void by constitutional or statutory provisions. Nearly all the cases assume this to be the rule, and do not discuss it. Even when a Constitution or statute declares such stock to be void, it is rarely possible to apply the statutory rule. A few cases speak of such stock as being void, but inasmuch as the remedies given in such cases are the remedies for the rescission of contracts for fraud, the stock involved was treated as being voidable for fraud, rather than void absolutely.¹

§ 26. *Constitutional provisions making it void.*—There have been various constitutional and statutory provisions on this subject in the different States. In some, the State Constitution provides that stock shall not be issued except for money, labor done, or money or property actually received, and that all fictitious increase of stock shall be void.² Such a provision is held to be

it was only as a fraud upon future creditors, that exception could be taken to an issue of stock at a discount. In *Lorillard v. Clyde*, 86 N. Y. 384 (1881), the court held it legal for the parties, as between themselves, to issue paid up stock for property taken at a valuation agreed upon between themselves. The court said: "If it had appeared that the organization of the corporation in this way, was a device to defraud the public, by putting valueless stock on the market, having an apparent basis only, a different question would be presented." See also *Otter v. Brevoort Co.*, 50 Barb. 247-

256 (1867), *dictum*; *Spring Co. v. Knowlton*, 103 U. S. 49-58 (1880), *dictum*.

¹ *Sturges v. Stetson*, 1 Biss. 246 (1858); *Fosdick v. Sturges*, 1 Biss. 255 (1858); *Gilman, Clinton & Springfield R. Co. v. Kelly*, 77 Ill. 426 (1875); *Campbell v. Morgan*, 4 Bradw. (Ill.) 100 (1879).

² Constitution of Ill. (1870), Art. XI, § 13; Neb. (1875), Art. XI, § 5; Mo. (1875), Art. XII, § 8; Penn. (1875), Art. XVI, § 7; Texas (1876), Art. XII, § 6; Colorado (1876), Art. XV, § 9; Arkansas, Art. XII, § 8; Alabama, Art. XIV, § 6; Louisiana (1879), Art. 238. In the last State any corporation issuing such stock shall forfeit its charter.

applicable and effective only when the issue is entirely fictitious. It does not interfere with the customary methods of starting the corporate enterprise by the issue of stock and bonds in payment for the construction of the corporate works. It may be said that these constitutional provisions have decidedly failed to remedy the evil which they were expected to cure.¹ They are so sweeping in their effects, and so disastrous to innocent holders of corporate securities that the courts are reluctant to declare void the stock and bonds issued by the corporation. The trouble with such remedies is, that they attempt to cure the evil after it has been consummated, instead of attempting to prevent its occurrence.²

¹ *Peoria & Springfield R. R. Co. v. Thompson*, 103 Ill. 187 (1882), the court, in interpreting this constitutional provision, said: "The object was doubtless to prevent reckless and unscrupulous speculators, under the guise or pretense of building a railroad, or of accomplishing some other legitimate corporate purpose, from fraudulently issuing and putting upon the market, bonds or stocks that do not and are not intended to represent money or property of any kind, either in possession or expectancy, the stock or bonds in such case being entirely fictitious. We cannot believe it was intended by the provisions in question to interfere with the usual and customary methods of raising funds by railroad companies for the purpose of building their roads, or of accomplishing other legitimate corporate purposes. . . . Under this provision of the constitution railroad companies have no right to lend, give away or sell on credit, their bonds or stock, nor have they the right to dispose of either, except for a present consideration and for a corporate purpose." In this case bonds and cash were given to the contractors in payment for the construction of the road. The transaction was upheld. In *California*, the Supreme Court, in *Stein v. Howard*, 65 Cal. 616 (1884), has held that the constitutional prohibition does not prevent the issue of stock at less than its par value. The meaning of "fictitious" is defined to be that given in Webster's Dictionary. The court said, "Of the shares proposed to be issued, *there is no one share* upon which a person can place his finger and say, that share is or will be feigned, imaginary, not real; counterfeit, false, not genuine." An injunction to restrain such an issue of new

increased stock was refused. In *New Castle R. R. Co. v. Simpson*, 21 Fed. Rep. 535 (1884), the court, in passing on the provision in the Pennsylvania constitution, held, that a contract giving a construction company \$300,000 of stock, and \$300,000 of bonds for work worth but \$180,000, will be set aside, although \$40,000 of work has been done. The construction company will be repaid the \$40,000 in cash.

² President Roberts of the Pennsylvania Railroad, is reported to have said (*New York Times*, October 4th, 1886): "If State Legislatures and Congress would pass proper laws for the protection of railroads, no pools would be necessary. We are common carriers, and it is proper enough that the Government should exercise supervision over us; but it should at the same time protect us by proper laws. Under the general railroad law of Pennsylvania and its recent amendments, the railroads of the State are at the mercy of speculators. Under the law any one can build a railroad and issue stocks and bonds to an unlimited extent, and at any rate to the amount of four or five times the cost of the road. These securities are solid. The road cannot earn the interest on its securities, and goes into bankruptcy. No responsible company can compete with an irresponsible company. No company managed by its owners can compete with one managed by a receiver. It makes no difference to the receiver whether the road he manages earns 5 cents or \$5." It is believed by the author that there is but one way of preventing the issue of fictitiously paid up stock. The law should prohibit all issues of stock for labor, property, or contract work, unless, before such issue,

§ 27. *Statutes making it void.*—Many of the States have statutes affecting the validity of stock issued as paid up, when its par value has not been actually paid in.¹ In New York, under the statute allowing the incorporation of manufacturing companies, it has been held that an issue of stock as paid up for cash, at less than its par value, is void.² In Ohio, by statute, an issue of stock to a director, directly or indirectly, for less than the par value thereof, is void.³ In some cases where the issue of paid up stock, in similar corporations, was for property taken at an overvaluation, it was assumed that the statute did not make the issue void.⁴

§ 28. *English statutes.*—In England, in 1863, the Companies Clauses Consolidation Act⁵ prohibited the issue of new stock for a price less than its par value. An amendment thereto in 1869⁶ struck out this prohibition, and gave power to the directors

it shall have been decided by a commission appointed by a specified court, that the labor, property, or contract work so received is equal in value to the par value of the stock issued for it. The method of procedure, appointment, powers, and duties of such a commission could be made to correspond largely with those of commissions appointed to condemn property under the power of eminent domain.

¹ Gen. Stat. of Mo., ch. 62, § 11, p. 328; 2 Rev. Stat. of N. Y. 507, § 49; 504, § 38; 505, §§ 40, 41; N. Y. Session Laws, 1848, ch. 40, §§ 38, 40, 41, 49. In Wisconsin the following remarkable statute exists, R. S., 1878, § 1753, as amended by ch. 93, Laws, 1881: "No corporation shall issue any stock, or certificate of stock, except in consideration of money, or labor, or property, estimated at its true money value, actually received by it, equal to the par value thereof . . . and all stocks and bonds issued contrary to the provisions of this section, and all stock dividends, or other fictitious increase of the capital stock of any corporation shall be void, provided, however, that any corporation whose stock or bonds have been, or shall hereafter be admitted to the stock exchange of Chicago, New York, Boston, or Philadelphia, or of either of said cities, may sell such stock or bonds so admitted at the best price or prices current for the time being obtainable therefor on any of the said exchanges at which the same shall be offered for sale."

² *Spring Co. v. Knowlton*, 103 U. S. 49 (1880); *Knowlton v. Congress & Empire Spring Co.*, 14 Blatchf. 364 (1877); *Knowlton v. Congress & Empire Spring Co.*, 57 N. Y. 518 (1874). These three decisions arise from the litigation of a single case. After being reversed in the New York court, it was removed into the Federal court. In all three decisions the invalidity of the stock was conceded by both parties. The Federal courts differed from the State courts, and held that a person partly paying for such illegal stock may recover back such payment, although he had allowed the stock to be forfeited for non-payment of further calls.

³ Section 3,313 of the Revised Statutes of Ohio sets forth that "all capital stocks, bonds, notes, or other securities of a company purchased of a company by a director thereof, either directly or indirectly, for less than the par value thereof, shall be null and void." In *Zabriskie v. Cleveland C. & C. R. Co.*, 23 How. 381 (1859), this provision was held not to affect the liability of a guarantor of such bonds. Under the foreclosure proceedings of the Nickel Plate Railroad, now pending in the court at Cleveland, Ohio, the stockholders seek to avoid the bonds and mortgage by the application of this statute.

⁴ See § 34.

⁵ See 8 & 9 Vic. c. 16, § 21.

⁶ See 32 & 33 Vic. c. 48, § 5.

to issue stock on such terms and conditions as they saw fit. The Railway Companies Act¹ of 1867 is to the same effect. Nevertheless, there seems to be no English case holding that an issue of stock at a discount is a transaction which, under all circumstances, is legal, valid, and binding on all parties.

§ 29. *Fictitious stock may be voidable.*—Is stock voidable when fraudulently issued as paid up? There are few cases on this question, but the tendency of the courts is to hold that such issues of stock may be avoided by a withdrawal of the issue and a cancellation of the certificates. Thus a court of equity, on the application of a dissenting stockholder, has decreed that stock falsely issued as paid up stock should be delivered up to the corporation for cancellation.² Where, however, the stock has passed into the hands of *bona fide* purchasers for value, such purchasers are entitled to retain the stock. Some cases intimate that the stock fictitiously issued may be cancelled, except a part whose par value would equal the amount actually paid in by the persons receiving it.³ Many cases hold also that the transaction is in the nature of a fraudulent contract, and that it may be rescinded for fraud, in which case the stock would have to be returned to the corporation.

So far as the right of the corporation to issue stock below par is concerned, the courts have frequently held that the issue is an *ultra vires* act.⁴ But an *ultra vires* act is not always void absolutely, and it is voidable only at the instance of persons standing

¹ See 30 & 31 Vic., c. 127, § 27.

² *Gilman, Clinton & Springfield R. R. Co. v. Kelly*, 77 Ill. 426 (1875). In this case it was admitted that the stock was issued gratuitously, and for the purpose of enabling the construction company to own a majority of the stock, thereby controlling the corporation.

³ *Sturges v. Stetson*, 1 Biss. 246-254 (1858). The court said, in a *dictum*, that stock taken at less than par with knowledge, is subject to the right of other stockholders, being such at the time of its issue, "to have it reduced to the charter value of the shares. This would take from him nearly one third of his shares." In *Fosdick v. Sturgis*, 1 Biss. 255 (1858), the court says there can be no question that this remedy is available.

⁴ *Fisk v. Chicago, Rock Island & Pac. R. R. Co.*, 53 Barb. 513 (1868), where the

court says: "It is not a question of good faith, or of honest intention, or of wise policy, or skillful or discreet management on the part of the directors. It is a question of power." In *West, & Co., R. v. Mowatt*, 12 Jur. pt. 1, 407 (1848), the court sustained a demurrer to a bill for specific performance of a contract to take shares from the corporation at a discount, the court holding that the contract was *ultra vires*. In *Ex parte Daniell*, 1 De Gex & Jones, 372, the court says: "It was very properly admitted . . . that the directors of the company had no power to pass the resolution" issuing the stock for less than its par value. In *Brown's Case*, 2 De Gex, F. & J. 275-295 (1860), it is held to be "beyond the functions and in excess of the powers" of the directors.

in a certain relation towards the act. Who can avoid the act will be explained hereafter.

§ 30. *First method of issue—By discount in cash.*—As already stated, paid up stock may be improperly issued in three different methods: by part cash payment; by taking property at an overvaluation; by an invalid stock dividend.

An issue of paid up stock for cash, upon payment of only part of the par value of the stock, is not often made, inasmuch as the real nature of the transaction is readily discovered and easily remedied. Sometimes the corporation makes the issue under a contract with those receiving it, that no more than a certain percentage of the par value will be called for. Again, the release is sometimes made by a resolution of the directors or stockholders, after subscriptions have been made and partly paid, discharging the subscribers from any further liability on such subscriptions. The proceedings are generally spread upon the corporate records; certificates are issued, asserting on their face that they are paid up; and all inquiries at the corporate office are answered by a substantiation of that assertion.

§ 31. *Dangers attending this method.*—There are various dangers and liabilities growing out of such a transaction. The stock is liable to be cancelled.¹ The person to whom it was issued,² or his transferee with notice,³ or the corporate officers participating in the act⁴ may, under certain circumstances, each be held liable personally for the unpaid par value of the stock. They may be liable to the corporation itself,⁵ or to the corporate creditors,⁶ or to *bona fide* transferees of the stock.⁷

A *bona fide* transferee of such stock, however, is not liable.⁸ But it has been held that the corporation may refuse to allow a transfer on the corporate transfer book of stock so issued.⁹

§ 32. *Rule in England sustaining issues below par.*—In England entirely different rules prevail on this subject so far as corporate creditors are concerned.¹⁰ It is held that where a contract for the issue of stock for cash at a discount is regularly reg-

¹ See § 29.

² See §§ 46, 47, and Chap. X.

³ See § 49.

⁴ See § 48.

⁵ See § 38.

⁶ See §§ 42-44.

⁷ See § 40.

⁸ See § 50.

⁹ *People v. Sterling Mfg. Co.*, 82 Ill. 457 (1876).

¹⁰ See § 44.

istered with the public registrar, as provided by statute, then the person to whom the stock is thus issued by contract as paid up stock is not liable to the corporation, nor corporate creditors, nor any other person for the unpaid par value of the stock, and his transferee is likewise protected.¹ In England such issues of stock are looked upon as matters of contract between the corporation and the person receiving the stock. Such a contract is valid as against the corporation and corporate creditors. Probably the only persons who could disturb it would be dissenting stockholders, being such at the time of the issue of the stock.

§ 33. *Second method—Issue of stock for property taken at an overvaluation.*—A second method of issuing stock as paid up, when it is not actually paid up, is by its issue for property taken at an overvaluation. This method is the most frequently employed, the most difficult to prove, and the least easy to remedy. A large amount of litigation and confusion has been experienced and gone through with, in determining the principles of law which should govern such transactions. The two questions which have perplexed the courts were, first, what constituted an overvaluation sufficient to invalidate the contract; second, what remedy should be applied when the contract was invalidated.

§ 34. *New York rule.*—In New York the Court of Appeals was at first in doubt whether proof of a mere overvaluation of the property was sufficient to set aside the payment as a full payment, or whether it was necessary for the plaintiff to prove also that the overvaluation was intentional and fraudulent.²

¹ *Re Ince Hall Rolling Mills Co.*, 30 W. R. 945 (1882), the court refused to hold liable the person receiving the stock, but in a *dictum* said: "Assuming that the contract was *ultra vires*, what would be the result? If it is *ultra vires* it must be set aside *in toto*, the consequence being that these gentlemen would be entitled to be relieved of their shares and receive back the money paid upon them." In the case of *Guest v. Worcester R. R. Co.*, L. R. 4 C. P. 9 (1868), where stock had been issued as paid up stock to a corporate creditor as security for his debt, nothing having been paid on such stock, the court said it did "not entertain a shadow of a doubt," and that the holder was not liable thereon. In *Baron De Beville's Case*, L. R. 7 Eq. Cas. 9 (1868), "paid up" shares had been issued to De Beville, who had

subscribed for "paid up" shares, but had paid no part of the par value thereof. The court held him not liable. In this case the corporation had authority to issue ordinary shares for cash, and "paid up" shares for property or services. *Ex parte Daniell*, 1 De Gex & Jones, 372 (1857), is not strictly in accordance with the preceding authorities, but in Daniell's case the issue was to a director who was acting in a fiduciary capacity. The case is so distinguished in *Carling's Case*, L. R. 1 Ch. D. 115 (1875).

² *Boynton v. Hatch*, 47 N. Y. 225 (1872). Three of the judges held that proof of fraud was necessary, and three that it was not necessary. All concurred in holding that proof of overvaluation was competent and necessary.

Later cases, however, as well as cases in other States, have firmly established the principle that not only must proof be given that there was an overvaluation of the property or services rendered, but proof also must be given that such overvaluation was intentional and consequently fraudulent.¹ The property is not to be considered as overvalued merely because, subsequently, it turns out to be so. The various circumstances under which the valuation was made should be considered in determining the *bona fides* of the transaction.²

The questions as to whether there was an overvaluation of the property, and whether that overvaluation was intentional and fraudulent are, generally, questions of fact to be submitted to the jury.³ Where, however, the overvaluation is so great as to bear evidence upon its face that it was intentional and fraudulent, the court will hold that, unless the transaction is reasonably explained, there is no question of fact for the jury, but that, as a matter of law, the overvaluation was fraudulent.⁴

¹ *Douglas v. Ireland*, 73 N. Y. 100 (1878); *Schenck v. Andrews*, 57 N. Y. 133 (1874); *Boynton v. Andrews*, 63 N. Y. 93 (1875); *Lake Superior Iron Co. v. Drexel*, 90 N. Y. 87 (1882); *Brant v. Ehlen*, 59 Md. 1 (1882). In the last case the court said: "So long as the transaction stands unimpeached for fraud, courts will treat as a payment that which the parties themselves have agreed shall be a payment, and this too in cases where the rights of creditors are involved." *New Haven, &c. Co. v. Linden Spring Co.*, 6 Eastern Rep. 663 (Mass. 1886).

² *Schenck v. Andrews*, 57 N. Y. 133 (1874). In *Coit v. North Car. Gold Amal. Co.*, 14 Fed. Rep. 12 (1882), the court said corporations "ought not to be made liable individually for the debts of the company at the instance of creditors, because, at a later day, the estimate fairly put upon the property at that time has become modified by subsequent events, and will not amount to the value which they set upon it." In *Carr v. Le Fevre*, 27 Pa. St. 413 (1856), the court said if the directors "took lands at a prospective value, never realized, it is nothing more than many individuals and corporations have done before. Such an error in management or in their judgment of the value of a purchase, made without fraud, forms no ground for rescinding the contract." See also *Schroder's Case*, L. R. 11 Eq. Cas. 131 (1870).

³ *Boynton v. Hatch*, 47 N. Y. 225 (1872); *Lake Superior Iron Co. v. Drexel*, 90 N. Y. 87 (1882).

⁴ Thus, where stock for \$300,000 was issued for property which the jury found to be worth \$64,000, the court held, as a presumption of law, that the transaction was fraudulent. *Douglas v. Ireland*, 73 N. Y. 100 (1878). In another case, involving the same facts, the trial court submitted the question to the jury. *Brockway v. Ireland*, 61 How. Pr. 372 (1880).

In another case, where stock for \$100,000 was issued for property worth not more than \$50,000, the court held, that in the absence of evidence to explain the presumption of fraud, there was no question for the jury, and that the transaction was fraudulent upon its face. *Boynton v. Andrews*, 63 N. Y., 93 (1875). An issue of \$190,000 of stock for property worth \$27,500, was held to be a fraudulent overvaluation, as a matter of law. *Osgood v. King*, 42 Iowa, 478 (1876). The case of *Lake Superior Iron Co. v. Drexel*, 90 N. Y. 87, tends to make the valuation of the property a question for the jury exclusively. In that case, stock for \$2,500,000 was issued for property in a patent. \$900,000 of the stock was returned to the corporation as a gift. The court held that the question of fraud was for the jury. This case was followed in *Draper v. Beadle*, 16 Weekly Dig. 475 (1883), Supm. Ct. N. Y. Gen. T. In *Bolz*

§ 35. *English statute and rules.*—In England, the issue of stock for property or services is largely regulated by statute. On account of the many frauds perpetrated upon the public by the issue of stock for property taken at a gross overvaluation, parliament, in 1867, passed an act requiring all contracts whereby stock was issued for property or services, to be publicly registered, under penalty of the payment being void.¹ Difficulty then arose as to what was the status and liability of a person receiving stock for property, in case the contract therefor was not publicly registered, as required by Act of Parliament. The courts finally decided that if the sums due reciprocally were expressly offset, then that the stock was to be deemed paid for, notwithstanding the statute.² But a mere general understanding that the property is payment for the stock is insufficient. The prohibition in the statute then applies, and payment in cash will have to be made upon a winding up.³ The point decided by these cases seems to have been misapprehended in a few American cases.⁴

In England, also, many cases sustain the rule that where fraud enters into an issue of stock for property, the party receiving the stock cannot be held liable for the par value thereof. The transaction, like other fraudulent agreements, may be set aside, and the parties restored to their original positions, but it must be rescinded *in toto* or adopted *in toto*.⁵

v. Ridder, 19 Weekly Dig. 463 (1884), N. Y. Com. Pl., the remarkable rise in value of a patent right from \$1,000 to \$100,000, when sold for stock issued in payment therefor, was held to be only presumptively fraudulent, and may be explained sufficiently to raise a question for the jury. The directors in estimating the value of property may take the opinion of experts, and rely thereon. *Brockway v. Ireland*, 61 How. Pr. 372 (1880). See also *Thurston v. Duffy*, 38 Hun, 327 (1885); *cf. Knowles v. Duffy*, 40 Hun, 485 (1886), properly holding differently from the last case on the same facts.

¹ 30 & 31 Vict. ch. 131, § 25. "Every share in any company shall be deemed and taken to have been issued and to be held subject to the payment of the whole amount thereof in cash, unless the same shall have been otherwise determined by a contract duly made, in writing, and filed with the Registrar of Joint-Stock Companies at or before the issue of such shares."

² *Pell's Case*, L. R. 5 Ch. App. 11 (1869); *Ex parte Clarke*, L. R. 7 Eq. Cas. 550 (1869); *Nicoll's Case*, L. R. 7 Ch. Div. 533 (1878). See also Chap. II. in *Spargo's Case*, L. R. 8 Ch. App. 407 (1873), the court said: "If the parties account with each other, and sums are stated to be due on one side, and sums to an equal amount due on the other side on that account, and those accounts are settled by both parties, it is exactly the same thing as if the sums due on both sides had been paid." See also *Maynard's Case*, 22 Week. R. 119; *Re Vulcan Iron Works*, Law Times, May, 1885, p. 61.

³ *Dent's Case*, L. R. 15 Eq. Cas. 407 (1873); *Fothergill's Case*, L. R. 8 Ch. App. 270 (1873); *Crickmer's Case*, L. R. 10 Ch. App. 614 (1875); *Rowland's Case*, 42 L. T., N. S., 785 (1880).

⁴ See *Wetherbee v. Baker*, 35 N. J. Eq. 501 (1882).

⁵ See §§ 47, 48.

§ 36. *Dangers of this method.*—When it has been established that the overvaluation of the property taken in payment of stock was intentional and fraudulent, and that the transaction was invalid, the questions then arise, what liability has been incurred, who is liable, and what is the remedy? The directors participating in the transaction may be held liable to the corporation for a breach of trust, but their liability is not to the extent of the par value of the stock, less the actual value of the property received, but is limited to the profit received by them, or by what the stock would actually have sold for in the market, less the value of the property received.¹ As regards the person receiving the stock for property taken at an overvaluation fraudulently made, the contract may be set aside for fraud, thereby returning to him the property and requiring from him the stock or its actual market value, but he is not liable for the par value of the stock less the actual value of the property received from him.²

§ 37. *Who may complain of an issue of stock as “paid up,” when it has not been fully paid?*—(a.) *The State.*—As already indicated, the issue of stock as paid up, when not actually paid up, is an act *ultra vires* of the corporation. The commission of *ultra vires* acts by a corporation, to the detriment of the public, renders its charter liable to forfeiture, at the instance of the State.

The issue of fictitiously paid up stock, with a view to defrauding the public, might constitute a misuse of the corporate rights and privileges. In such a case it is not clear but that the State might proceed to forfeit the charter of the corporation.³

Again it is a principle of law that when a corporation is guilty of an *ultra vires* act, and such act is detrimental to the interests of the public, it is competent for the Attorney-General to file an information for the purpose of enjoining or setting aside such act.⁴

Under this rule, it would seem that the Attorney-General might effectively enjoin or set aside an irregular issue of paid up stock.

¹ See § 48.

² See §§ 46, 47.

³ In *Holman v. State, &c.*, 5 Northeast. Rep. (Ind. 1886) the State caused a charter to be forfeited because the subscribers for stock were insolvent at the time of

subscribing, thereby perpetrating a fraud on the public. See also *Jersey City G. L. Co. v. Dwight*, 29 N. J. Eq. 242; *Erie Ry. Co. v. Casey*, 26 Pa. St. R. 287-318 (1856).

⁴ Green's *Brice's Ultra Vires*, 3d ed. pp. 708, 709.

§ 38. (b.) *The corporation itself.*—The corporation itself, after issuing its stock as paid up stock, and declaring it so to be, cannot subsequently repudiate that declaration and agreement and proceed to collect the unpaid part of the par value, either from the person receiving the stock, or his transferee. It is estopped from so doing.¹

Where, however, fraud enters into the transaction, then, it seems, the corporation is not estopped from having the agreement set aside. The person receiving the stock can then be compelled to return the stock, or its market value, and take back that which he gave to the corporation for it. The corporation cannot hold him liable for the par value of the stock.²

The corporation has also a remedy herein against its directors who issued the stock either fraudulently or in an *ultra vires* manner.³ This liability is similar to their general liability to the corporation for fraudulent, negligent, or *ultra vires* acts on their part.⁴ The measure of their liability, herein, is not the par value of the stock, less the value actually received therefor by the corporation, but it is the actual value of the stock, generally the market value, less the property or cash actually received by the corporation on the stock so issued.

It has also been held that the corporation cannot, in a court

¹ In the case of *Scoville v. Thayer*, 105 U. S. 143 (1880), the court said, in a *dictum*: "No call could have been made by the company under its agreement with the shareholders, unless to pay its creditors. . . . The shares were issued as paid up, on a fair understanding, and that bound the company." The issue had been at a discount.

See also *Union, &c., Co. v. Frear, &c.*, Co. 97 Ill. 537 (1881), *dictum*. In the case of *Granite Roofing, &c., Co. v. Michael*, 54 Md. 65 (1880), stock was issued as paid up for cash, although not actually paid. The corporation passed under the control of purchasers of the stock, who caused the corporation to sue the original subscribers for the unpaid par value of the stock. The court said: "While the law may reject, as illegal and fraudulent, that which the parties have agreed upon, . . . it will not arbitrarily incorporate, in lieu thereof, terms in the contract to which the parties have never assented." In the case *Re Ambrose L. T. & C. Mining Co.* L. R. 14 Ch. Div. 390 (1880), where all

the stockholders acquiesced and there were no creditors' rights involved, the court held that the corporation could not hold the directors liable for the profits made by them. In *Zirkel v. Joliet Opera House Co.* 79 Ill. 334 (1875) the corporation had released the subscriber after the subscription had been made. The release being without consideration, and not a contract, was held void, and the corporation was allowed to recover. The case of *The Society of Prac. Knowl. v. Abbott*, 2 Beav. 559 (1840), was distinguished in *Re British S. P. B. Co.*, L. R. 17 Ch. D. 467 (1881), the latter case holding that no one is liable on fictitiously paid up stock where all acquiesced and there was no intent to bring in new stockholders, even though new ones were subsequently brought in. See also *Flinn v. Bagley*, 7 Fed. Rep. 785 (1881); *Re Glen Iron Works*, 17 Fed. Rep. 24 (1888); *cf. People v. Sterling Mfg. Co.* 82 Ill. 457 (1876).

² See §§ 47, 48.

³ See § 48.

⁴ See Part IV.

of equity, compel a person, who agreed to take stock at a discount, to carry out the contract, inasmuch as it is *ultra vires*.¹

§ 39. (c.) *Stockholders participating in the act cannot complain*.—Stockholders in a corporation, who participate or aid in the issue of paid up stock, upon payment of less than its par value, or who have knowledge of the act and acquiesce therein, cannot afterwards complain of the transaction, either in their own behalf or in behalf of the corporation. They are bound by estoppel or acquiescence.²

The cases are in conflict on the question whether the party receiving stock at a partial discount of its par value, may repudiate the transaction and recover from the corporation the money he has already paid thereon.³ Where the stockholders participating in the issue disagree among themselves as to the division of the stock, the courts will not render aid to one as against the others.⁴

§ 40. (d.) *Transferees of participating stockholders*.—Not only the participating and acquiescing stockholders, but also their transferees are bound by the participation or acquiescence. The transferee cannot claim to have greater rights than his transferer, as regards a general remedy invalidating the whole transaction. He cannot bring suit in behalf of the corporation and other stockholders against the party or parties participating in the issue, in-

¹ West. R. R. Co. v. Mowatt, 12 Jur. pt. I, 407 (1848).

² In *Re Gold Co. L. R.* 2 Ch. Div. 701-712, the court says: "It could not be a fraud upon, or a wrong to the existing stockholders, because every one of them was a party to the transaction." See also *Scoville v. Thayer*, 105 U. S. 143 (1881). But in the case of *Knowlton v. Congress & Empire Spring Co.* 14 Blatchf. 364-368 (1877), the court said, in a *dictum*: "Can there be any doubt that up to the time of the abandonment of the scheme by the defendant, the plaintiff could have resorted to a court of equity and restrained further proceedings and vacated the proceedings already taken? The cases are numerous where courts of equity have interfered to prevent the consummation of a wrong, upon the motion of a party who was instrumental in its inception." *Aff'd*, 103 U. S. 49. The issue of stock in that case was held to be absolutely void by statute.

³ The case of *Clarke v. Lincoln Lumber Co.* 49 Wis. 655 (1884), holds that a participating subscriber cannot withdraw and recover back sums already paid. See also *Goff v. Hawkeye P. & W. Co.* 62 Iowa, 691 (1883). *Knowlton v. Congress & Empire Spring Co.* 57 N. Y. 518-537 (1874), holds the same, the court saying: "Such parties are left in the position they have placed themselves." The latter case was decided otherwise in the Federal courts (14 Blatchf. 364, and 103 U. S. 49), it being there held that a recovery might be had, where others are repaid.

Mandamus will not issue to compel the issue of stock at a discount, in performance of a resolution by the stockholders that such issue shall be made. Equity will not aid the fraud. *State v. Timken* (N. J. 1886), 3 Central Rep. 212.

⁴ *Tobey v. Robinson*, 99 Ill. 202 (1881).

asmuch as his own title is tainted with the same fraud.¹ Nor can he bring an action against the corporation.² But the transferee is by no means without a remedy. He may bring an action for damages against those who, knowing the facts, induced him to purchase, or those who made it possible for the fraud to be practiced, or who actually assisted in perpetrating the fraud upon him.³

The transferee has other remedies. If the transfer to him was from one of the participants, he may rescind the transfer and recover back the price paid by him;⁴ or, if the contract of purchase is not yet completed, he may refuse to take the stock.⁵

¹ *Parsons v. Hays*, 14 Abb. N. C. 419 (Super. Ct. 1883); *Nott v. Clews*, 14 Abb. New Cases (N. Y.), 437; *Flagler Co. v. Flagler*, 19 Fed. Rep. 468 (1884, Circ. Ct. Mass.); s. c. 14 Abb. New Cases (N. Y.), 435. See also *Langdon v. Fogg*, 18 Fed. Rep. 5 (1883). In the late case of *Foster v. Seymour*, 23 Fed. Rep. 65 (1885, U. S. Circ. Ct. Wallace, J.), an issue of stock for property at an overvaluation is distinctly held to be no fraud upon the corporation, nor upon the stockholders, all of whom participated. "A purchaser of the stock would not be injured by the transaction unless he paid more for it than it was worth; and every purchaser would stand upon the particular circumstances of his purchase." A suit against the guilty parties, who were the directors, to compel them to account for a fraudulent disposition of corporate property will not lie. The fraud is not corporate; it is personal.

² In *Re Gold Co. L. R.* 11 Ch. D. 701 (1879), the court said: "It was not a wrong done by the company or to the company." In *Re Ambrose Lake T. & C. Min. Co. L. R.* 14 Ch. D. 390-397 (1880), the court says: "There would be no liability on the part of the company, as such."

³ The leading case on this principle of law is *Cross v. Sackett*, 6 Abb. Pr. R. 247 (1858), argued by eminent counsel and decided by learned judges. A *bona fide* purchaser, in open market, from an innocent holder, of stock issued as paid up for property taken at an overvaluation, sued a director, being also an original stockholder, for damages. The court held: "When a party projects and publicly promulgates the scheme of a joint stock company; when he causes the usual books to be opened, and allows or causes the inscription of a person as an owner of an interest to a definite amount and value

therein, which is false within his own knowledge; when he embodies such false statements in a certificate of this right directly issued and of the same effect as if signed by himself; when he accompanies that certificate by a written power authorizing a transfer at large, by the party to whom he has given the certificate; when that representation induces an innocent person to advance his money—the defendant's own individual act has created the privity of contract . . . and he must be held responsible to any one who has been deceived."

The plaintiff must prove that a representation was made that the stock was paid up, and that he relied thereon, and that the representation was false and fraudulent. *McAleer v. McMurray*, 58 Penn. St. 126 (1868); *Priest v. White*, 34 Alb. L. J. 298 (1886).

The court in *In re Ambrose Lake Tin & Cop. Min. Co. L. R.* 14 Ch. D. 390-397 (1880), said that the transferee has a remedy against the person who, in any way, made the misrepresentations to him. *Re Gold Co. L. R.* 11 Ch. D. 701, pp. 713, 714, is to the same effect. In *Barnes v. Brown*, 80 N. Y. 527 (1880), the plaintiff, being under contract to receive paid up stock from defendants, received such, and afterwards discovered that its par value had not been paid in to the corporation. The court held that he could recover damages from the defendant for the fraud, in which he had participated:

⁴ *Fosdick v. Sturges*, 1 Biss. 255 (1858). In this case the certificate was brought into court to be disposed of as the court should direct.

⁵ *Sturges v. Stetson*, 1 Biss. 246-253 (1858), the court holding that an action for the price of such stock is in the nature of a bill in equity for the specific performance of a contract, and the defendant may

§ 41. (e.) *Stockholders dissenting at the time of the issue may complain.*—Stockholders, being such when an issue of paid up stock is improperly made, and not assenting to or acquiescing in it, may bring suit in a court of equity to annul and set aside the whole transaction.¹ It has been held that the issue may be cancelled.² The dissenting stockholders' rights and remedies herein, in their scope and details, are similar to the rights and remedies of stockholders in other cases of *ultra vires* acts or fraud to the injury of the corporation, a subject fully treated in the fourth part of this work.

§ 42. (f.) *Corporate creditors as complainants where the issue is for money.*—According to well established rules of law in America, corporate creditors may object to certain transactions, which, as between the corporation and its stockholders and third persons, may be valid and binding. This right of corporate creditors is an essentially American doctrine. It is based on the principle, first enunciated by Judge Story, that the capital stock of the corporation is a trust fund, to be preserved for the benefit of corporate creditors. That principle of law, when applied to a transaction, whereby stock is issued as paid up, when it is, in fact, not paid up, enables corporate creditors to object to the act, and, in certain cases, to undo what has been done, and, in other cases, to compel payment of the actually unpaid part of the par value of the stock. Where the issue of stock was for cash, under an agreement that only part of the par value need be paid, corporate creditors may compel the persons receiving the stock to pay the unpaid full par value.³

defeat it by avoiding the contract altogether, although the certificates have been transferred to him. To same effect, *Coolidge v. Goddard*, 77 Me. 579.

¹ In *Fisk v. Chicago & Rock Isl. R. Co.*, 53 Barb. 513 (1868), the court enjoined any transfer of the stock, and appointed a receiver to receive what the corporation had realized from the stock, and to use the funds in retiring the stock and paying damages caused thereby. In *Sturges v. Stetson*, 1 Biss. 246-254 (1858), and *Fosdick v. Sturges*, 1 Biss. 255-259 (1858), the court in *dicta* said that the issue could be withdrawn, leaving with the guilty party so much stock as the money paid by them would equal the par value thereof.

² *Campbell v. Morgan*, 4 Bradw. (Ill.) 100 (1879); *Gilman, Peoria & Spring. R. R. Co. v. Kelly*, 77 Ill. 426 (1875).

³ The leading case on this point is *Sagory v. Dubois*, 3 Sandf. Ch. Rep. 466-499 (1846), where the court said: "The defendant being liable by force of his subscription for the stock, the resolution of the directors . . . not to make any further calls upon the shares, was unavailing to discharge his liability in respect of the association and its creditors." In *Scoville v. Thayer*, 105 U. S. 143 (1881), the court said that a contract whereby stockholders are to pay but part of the par value of their stock to the corporation, "though binding on the company, is a fraud in law on its creditors, which they

But the amount collected must be to the extent and for the purpose of paying corporate creditors' claims only.¹ A resolution discharging stockholders from all liability on stock, after thirty per cent. of the par value has been paid, and then suffering a forfeiture of the stock, is void so far as corporate creditors are concerned.² In New York, this liability to corporate creditors is embodied in the statutes.³ In order to enforce this liability it is not necessary to prove that fraud entered into the transaction, where the issue was for cash, since there is no possibility of mistaken judgment in the value of the thing received in payment.⁴ Where the capital stock of the corporation is increased, the increase is not a trust fund for the benefit of corporate creditors, who were such before the increase was made.⁵ It has been held that the custom of the country will exempt stockholders from liability on stock issued as paid up, when it was not paid up. Such a decision, however, is inconsistent with the great weight of authority and must be considered poor law.⁶

§ 43. In England an entirely different rule prevails as regards the right of corporate creditors to collect the unpaid par value of stock issued for cash. Corporate creditors in England cannot enforce any liability which the corporation itself is estopped

can set aside; when their rights intervene and their claims are to be satisfied, the stockholders can be required to pay their stock in full." *Upton v. Tribilcock*, 91 U. S. 45 (1875), is the first of a series of cases growing out of the failure of the Great Western Insurance Co. of Illinois. The other cases are *Sanger v. Upton*, 91 U. S. 56 (1875); *Webster v. Upton*, 91 U. S. 65 (1875); *Chubb v. Upton*, 95 U. S. 666 (1877); *Pullman v. Upton*, 96 U. S. 328 (1877); *Hawley v. Upton*, 102 U. S. 314 (1880); *Upton v. Burnham*, 3 Biss. 431 (1873); s. c. 3 Biss. 520, and *Upton v. Hansbrough*, 3 Biss. 417 (1873). This series of cases established for the Federal courts the rule given above. See also *Flinn v. Bagley*, 7 Fed. Rep. 785 (1881), giving full review of the American and English doctrine herein. *In re Glen Iron Works*, 17 Fed. Rep. 374 (1883); *Union M. L. Ins. Co. v. Frear Stone Mfg. Co.*, 97 Ill. 537 (1881), also reviewing the doctrine; *Hickling v. Wilson*, 104 Ill. 54 (1882); *Northrop v. Bushnell*, 38 Conn. 498 (1871); *Fisher v. Seligman*, 7 Mo. App. 383 (1879); *Eyermaier v. Kriekhaus*, 7 Mo. App. 455 (1879); *Skrainka v. Allen*,

7 Mo. App. 434 (1879); *Pickering v. Templeton*, 2 Mo. App. 424 (1876); *Christensen v. Eno*, 21 Weekly Dig. 202 (1885); *Mann v. Cooke*, 20 Conn. 178 (1850); *Myers v. Suley*, 10 Natl. Bank. Reg. 411. As affecting corporate creditors herein, the Statute of Limitations does not commence to run until judgment is recovered by the corporate creditors against the corporation. *Christensen v. Quintard*, 36 Hun, 334 (1885).

¹ *Scoville v. Thayer*, 105 U. S. 143-155 (1881).

² *Slee v. Bloom*, 19 Johns. Rep. 456 (1822).

³ 1 R. S., Ch. 18, Title 3, § 5; N. Y. Session Laws, 1850, Ch. 140, § 10; *Id.* 1854, Ch. 282, § 16.

⁴ *Flinn v. Bagley*, 7 Fed. Rep. 785 (1881).

⁵ *Coit v. North Car. Gold Amal. Co.*, 14 Fed. Rep. 12 (1882).

⁶ *Re South Mountain Consol. Min. Co.*, 7 Sawyer, 30 (1881). In this case it is stated that corporate creditors were protected "by the personal liability of each shareholder for his *pro rata* share of the indebtedness of the corporation."

from enforcing.¹ The principle of law, that the capital stock of a corporation is a trust fund, to be preserved for the benefit of corporate creditors, is a distinctively American doctrine, and has never been recognized in England. Formerly the English courts were inclined to hold, that where paid up stock is issued under an agreement that but part of its par value need be paid, payment being in cash, that such agreement could be disregarded and the full par value collected. Later decisions repudiate this rule, and hold that there is no liability for the unpaid par value, and that the issue under the agreement is valid, unless impeached for actual fraud, and in that case it must be rescinded *in toto* or not at all.² In England, where the issue is for property taken at an overvaluation, the rights and remedies of the parties are the same as in America.³

§ 44. *Corporate creditors as complainants where the issue is for property or construction work.*—The rights of corporate creditors are not clear and certain where paid up stock was issued in consideration of property taken at an overvaluation. In order to reach the person receiving paid up stock for property, the corporate creditor must prove three things. He must prove that the property was overvalued, and unreasonably overvalued, since, if the estimate was a fair one when made, subsequent events cannot impeach it, even for the benefit of corporate creditors.⁴

The corporate creditor must also prove that the overvaluation was intentional and fraudulent. Until that is done the courts refuse to interfere with or set aside the discretion which has been exercised by the corporate authorities in valuing the property received.⁵ In the third place, the corporate creditor must prove

¹ In *Re Dronfield Silkstone Coal Co.*, L. R., 17 Ch. Div. 76 (1880), on p. 97, the court says: "If the company could not question it, neither can a creditor, for he can obtain nothing but what the company can get from the shareholders." See also *Re Ambrose Lake T. & C. Min. Co.*, L. R., 14 Ch. D. 390 (1880); *Re Ince Hall Rolling Mills Co.*, 30 W. R. 945 (1882), where the court said the same as in the preceding case. In *Waterhouse v. Jamieson*, L. R., 2 H. L. (Sc.) 29, the court said, p. 37: "I take it to be quite settled that the rights of creditors against the shareholders of a company, when enforced by a liquidator, must be enforced by him in right of the company;

what is to be paid by the shareholders is to be recovered in that right." Cf. remarks of the Lord Chancellor, p. 32.

² See § 32.

³ See § 35.

⁴ *Coit v. North Car. Gold Amal. Co.*, 14 Fed. Rep. 12 (1882). See also § 34.

⁵ In *Phelan v. Hazard*, 3 Dill. 45 (1878), Judge Dillon thoroughly reviews the authorities, and says: "The contract is valid and binding upon the corporation and the original shareholders unless it is rescinded or set aside for fraud, and . . . while the contract stands unimpeached, the courts, even where the rights of creditors are involved, will treat *that* as a payment which the parties have agreed should be

that the person so receiving the stock has made a profit therefrom. The transaction, being a fraudulent one, is rectified by the corporation returning the property, and the stockholder returning the stock or the real market or actual value thereof. He cannot be made liable for the par value of the stock less the real value of the property.¹

§ 45. *Who is liable, and the character of the liability. (a.) The corporation.*—The corporation itself, it has been intimated, is not liable to any person by reason of the issue of its stock as full-paid stock, when, as a matter of fact, it has not been fully paid.² It is very certain that the stockholder has no remedy herein against the corporation, since his remedy is against the corporate officers, as in other cases of breach of trust by them. As regards corporate creditors, they cannot complain provided the corporation remain solvent and able to pay its debts. If, on the other hand, it becomes insolvent, it would be no object to bring suit against the corporation.

§ 46. *(b.) Persons receiving the stock from the corporation.*—These are the ones against whom suit is generally brought. Their liability, under the various circumstances of the particular issue of stock has been explained elsewhere. Where the issue was for cash, they are liable, in America, to corporate creditors for the unpaid par value of the stock.³ In England they are not so liable.⁴ In either country the transaction may be rescinded and set aside *in toto* for fraud. Where the issue was for property taken at an overvaluation, the rules in America and England are the same. The transaction stands, and no liability is incurred unless an intentional overvaluation is proved.⁵ In that case a

payment." See also *Brant v. Ehlen*, 59 Md. 1 (1882), fully explaining the meaning of the term trust fund as applied herein. *Crawford v. Rohrer*, 59 Md. 599 (1882).

¹ See §§ 47, 48.

² In the case of *In re Ambrose L. T. & Cop. Min. Co.*, L. R. 14 Ch. D. 390-397 (1880), the court says: "There would be no liability on the part of the company as such." *In re Gold Co.*, L. R. 11 Ch. D. 701 (1879), where the proceeding was to compel a winding up of the company on account of an improper issue of paid up stock. The court refused to support the proceeding, and said, pp. 713-14, "it was

not a wrong done by the company or to the company." It has been held, however, in general, that "A corporation may be, in a legal sense, guilty of a fraud. As a mere legal entity it can have no will and cannot act at all, but in its relations to the public it is represented by its officers and agents, and their fraud in the course of the corporate dealings is in law the fraud of the corporation." *Cragie v. Hadley*, 99 N. Y. 131 (1885). See also *Lewis v. Meier*, 14 Fed. Rep. 311 (1882).

³ See § 42.

⁴ See § 43.

⁵ See § 34 *et seq.* For the remedy in that case see § 44.

dissenting stockholder, being such at the time of the issue, may have the transaction set aside, and the person receiving the stock compelled to return it or pay over its actual or market value, less the value of property given for it.¹ A corporate creditor in America may likewise bring an action for that purpose upon the insolvency of the corporation.² The person receiving stock at a discount is liable also to a *bona fide* transferee of that stock.³ A representation of the corporate agents to the person receiving the stock, that full payment will not be required, is immaterial, and constitutes no defense.⁴

§ 47. Many attempts have been made, in cases where stock was issued for property taken at an overvaluation, to hold the party receiving such stock liable for its full par value, less the actual value of the property received from him. These attempts have not been successful. As already seen, the transaction is upheld as legal, valid, and binding on all parties and persons, unless there is an overvaluation, and that overvaluation is shown to have been fraudulent. When this is proved, then the contract is to be treated like other fraudulent contracts. It is to be adopted *in toto*, or rescinded *in toto* and set aside. Each party is to be restored as nearly as possible to their original positions. The property or its value is to be returned to the person receiving the stock, and he must return the stock or its real value. Its real value is ascertained, not by its par value, but by its selling market value. Frequently actions herein are against corporate officers who directly or indirectly received the stock. Yet, notwithstanding that a breach of trust is thereby added to the fraud, the principles stated above have been uniformly applied.⁵

¹ See § 41.

² See § 44.

³ See § 40, and *Fisher v. Seligman*, 7 Mo. App. 383 (1879).

⁴ *Upton v. Tribilcock*, 91 U. S. 45 (1875); *Ogilvie v. Knox Ins. Co.*, 22 How. 380 (1859).

⁵ In *Anderson's Case*, L. R. 7 Ch. D. 75, stock was issued to a promoter for property taken at an overvaluation. This action was to render him liable for the par value of the stock, less the real value of the property. The court said, pp. 94, 95-104: "I am not going to alter men's contracts unless the provisions of an Act of Parliament compel me to do so. . . . You cannot alter the contract to such

an extent as to say, though you have bargained for paid up shares, we will change that into a bargain to take shares not paid up, and put you on the list of contributors on that ground. . . . If you set aside this allotment of shares, you must set it aside altogether, and then you cannot make them a contributory; and if you do not set it aside altogether you must adopt it, and the utmost you can do is, as I said before, that you can take away any profit from the person who has improperly made it." In *Currie's Case*, 3 De G., J. & S. 367 (1863), the court said that the transaction "was either valid or invalid. If valid, it is clear that neither he [the person receiving the stock] nor his alien-

§ 48. (c.) *The officers of the corporation.*—Corporate officers who aid in the issue of stock as paid up, when in fact its par value has not been fully paid, are liable to the corporation itself for a breach of trust in the performance of their corporate duties. Ordinarily the extent of his liability is the excess of the real or market value of the stock over the value received for it in its issue at a discount. But where the director or officer participated in the profits of the issue, he then is liable to the corporation for the profits which he has received.¹ The officers of a corporation par-

ees can be called upon to contribute in respect of those shares. If invalid, I cannot see my way to hold that either a court of law or a court of equity could do more than treat the purchase as void, and undo the transaction altogether. It could not, as I apprehend, be competent either to a court of law or to a court of equity to alter the terms of the purchase, or treat as shares not paid up, shares which were given as paid up shares in part consideration of the purchase. Fraud, assuming there was fraud, would of course warrant the court in treating the purchase as void, or in undoing it; but it could not, I conceive, authorize any court to substitute other terms." See also *Barnett's Case*, L. R. 18 Eq. 507 (1874), where the issue had been cancelled by the corporation. In *Van Cott v. Van Brunt*, 82 N. Y. 535 (1880), a case very similar in its facts to those of the preceding case, the court said: "The conclusion of law was erroneous that the scheme was fraudulent as against the company and against the creditors, and that the defendants were only entitled to credit for the actual outlay, paid or incurred, and were liable for the amount unpaid on the stock. The result must be that the defendant was not liable to pay the par value of the stock received by him under the contract for building and equipping a portion of the road," p. 542. This case has been severely criticised as being contrary to established principles of law. It would seem, on the contrary, that it not only is in accordance with general principles of law governing the rescission of contracts, but that it is in strict accordance with the authorities and cases on the subject of paid up stock. See also *Continental Telegraph Co. v. Nelson*, 18 Weekly Dig. 48 (1883); s. c. 49 N. Y. Super. Ct. 197; *Crawford v. Rohrer*, 59 Md. 599 (1882); *Brant v. Ehlen*, 59 Md. 1 (1882). Judge Dillon, in *Phelan v. Hazard*, 5 Dill. 45, reviewed the authorities

and sustained the principles enunciated herein. Before any recovery can be had in this class of cases the transaction must be set aside. *Scoville v. Thayer*, 105 U. S. 143-156 (1881); *Wood's Claim*, 9 W. R. 366 (1861). It has been held that the person then receiving the stock then becomes liable for profits made by him. *Four Mile V. R. R. Co. v. Bailey*, 18 O. St. 208 (1868). A few cases seem to be in conflict with the above authorities, but only apparently so. Thus, in *Wetherbee v. Baker*, 35 N. J. Eq. 501 (1882), the defendant neither owned nor conveyed to the corporation, the property which he alleged constituted payment. In *Jackson v. Traer*, 20 Northw. Rep. n. s. 764 (1884), overruling s. c. 16 Northw. Rep. n. s. 120 (1884), the stock was not issued to the construction company for the purpose of constructing the corporate works, but was issued after the construction was finished, and a cash debt was due them, which was paid by an issue of the stock to pay that debt already due. *Savage v. Ball*, 17 N. J. Eq. 142 (1864), held that the validity of an election is not affected by the question whether the stock voted was issued for value or not. In *Chisholm Bros. v. Forney*, 65 Iowa, 140 (1884), where full paid stock was issued for a patent right, in good faith, but the patent right subsequently turned out to be worthless, the stockholders were held liable to corporate creditors as though no payment had been made. This case does not coincide with the authorities, although it seems to accord with the tendency of the Iowa decisions.

¹ In *Douglass v. Ireland*, 73 N. Y. 100 (1878), where the person receiving the stock divided the profits of the transaction with the directors, the court held that the facts went very far in proving a breach of trust on the part of the directors. In *Anderson's Case*, L. R. 7 Ch. D. 75-94, the court held that if shares were

ticipating in the issue of stock as paid up, when it has not been fully paid, are liable also to persons purchasing such stock, for damage thereby suffered.¹ In Massachusetts, by statute, corporate officers are made liable for corporate debts, if they issue stock for property at an unfair valuation of the latter.²

§ 49. (*d.*) *Persons purchasing the stock with notice.*—It seems to be generally assumed, as a matter of course, that persons purchasing stock, with notice that it had not been paid up, although, in fact, it had issued as paid up, are liable on such stock to the same extent that their transferers were liable.³

§ 50. (*e.*) *Bona fide transferees without notice.*—A *bona fide* purchaser for value and without notice of stock issued by a cor-

improperly issued to a director at a discount, the contract might be set aside and the consideration returned, or the profits realized by him might be recovered. In *Currie's Case*, 3 De Gex, J. & S. 367 (1863), where shares were taken both directly and indirectly by the corporate officers for property and services grossly overvalued, the court held that the transaction might be undone altogether for fraud, but there was no liability on their part to contribute anything on the shares. The only remedy is to set aside the transaction and recover the profits thereof. In *Carling's Case*, L. R. 1 Ch. D. 115 (1876), where the person receiving stock for property taken at an overvaluation gave part of it to a corporate director, the court held that the corporation could demand of the director either the stock, or the profits realized by him, or the profits thereby lost by the corporation, but could not compel him to pay the full par value of the stock. In *De Ruigne's Case*, L. R. 5 Ch. D. 316 (1876), where shares of stock were issued as paid up to a person for services palpably overvalued, and he transferred a part of the stock to a director, *De Ruigne*, the court said: "If the company attempt to make the appellant [director] a contributory, and they allege fraud in the original agreement by which he was to take the shares, they must either throw over the agreement altogether, or they must take it altogether; they cannot adopt it as to one part and reject it as to the rest." The court said the director could be held liable for breach of trust and be made to pay to the corporation the selling value of the shares,

and since some of the stock was sold at par, he was chargeable with the par value of the stock so received by him. See also *Osgood v. King*, 42 Iowa, 478 (1876); *Flagler Engr. Machine Co. v. Flagler*, 19 Fed. Rep. 468 (1884); *Nott v. Clews*, 14 Abb. New Cases (N. Y.), 437; *Continental Tel. Co. v. Nelson*, 49 N. Y. Superior Ct. Rep. 197 (1884); and compare *Langdon v. Fogg*, 18 Fed. Rep. 5 (1883); s. c. 14 Abb. New Cases (N. Y.), 435. In the case of *Re Ambrose Lake T. & C. Min. Co.*, L. R. 14 Ch. D. 390 (1880), it was held that where all the stockholders acquiesced, and there were no creditors' rights involved, the corporation cannot recover from its directors profits realized by them from shares issued to them as paid up in consideration of property taken at a gross overvaluation. The corporation was held to be in no position to complain. In *Van Cott v. Van Brunt*, 82 N. Y. 535 (1880), where the facts were very much the same as in the preceding case, the court said: "If the defendant [director and president] had realized a sum beyond the amount actually expended, there might have been, perhaps, some ground for claiming that the arrangement would enure to and for the benefit of the company," p. 541. This remedy, it seems, is the surest and most just.

¹ *Cross v. Sackett*, 6 Abb. Pr. 247 (1858); *Re Gold Co.*, 11 Ch. D. 701, § 48.

² Statutes of Mass., Acts of 1875, Ch. 177, § 2.

³ *Upton v. Tribilcock*, 91 U. S. 45 (1875).

poration as paid up, cannot be held liable on such stock in any way, either to the corporation, corporate creditors, or other persons, should it be found that the stock was not actually paid up as represented. Such a purchaser has a right to rely on the representations of the corporation that the stock is paid up. Difficulty sometimes arises in determining what will constitute a sufficient representation that the stock is paid up. A representation by the corporate agents that the full par value will not be required is insufficient.¹ The word "non-assessable" stamped, or printed, or written on the face of the certificate, is not a sufficient representation that the stock is paid up, so as to protect a *bona fide* purchaser thereof.²

Where, however, a statement is made on the face of the certificate that it represents paid up stock, the *bona fide* purchaser of the certificate need not inquire further, but may rely on that representation, and is protected thereby against liability.³

A purchaser of stock is entitled to rely on statements in the corporate books that the stock is paid up.⁴ A few cases go still farther, and hold that where a person in open market, in good faith and without notice, purchases certificates, such stock is to be

¹ Webster v. Upton, 91 U. S. 65 (1875); Upton v. Tribilcock, 91 U. S. 45 (1875).

² Upton v. Burnham, 3 Biss. 431 (1873).

³ In Waterhouse v. Jamieson, L. R. 2 H. L. (Sc.), 29, where the stock was purchased in open market, the court said: "Here the appellant is a *bona fide* holder of shares, upon which, no doubt, there was a false statement made by the company, of which he had no knowledge, and as to which he was under no obligations to inquire, and therefore he cannot be subjected to liability by having imputed to him a knowledge of the falsehood." In Brant v. Ehlen, 59 Md. 1 (1882), the court said: "Where shares are issued by the company to the subscriber as full paid shares, and are sold by the subscriber as such, there is no ground on which a promise can be implied on the part of the purchaser without notice, to be answerable either to the company or its creditors, should the representations on the faith of which he purchased prove to be false. He could not be held liable on the ground of contract, because he never agreed to purchase any other shares than full paid

shares; and if it be said that the shares were fraudulently issued, he could not be held liable on the ground of fraud, because he was in no sense a party to the fraud." In Steacy v. Little Rock & Ft. Smith R. R. Co., 5 Dill. 348 (1879), Judge Dillon examined, at considerable length, the reasons of the rule protecting *bona fide* purchasers of stock issued as paid up, and sustained the rule itself. See also Burkinshaw v. Nichols, L. R. 3 App. Cas. 1004 (1878). One case, Myers v. Seeley, 10 Nat'l Bankr. Reg. 411, lays down a different doctrine. The court says: "The assignee of shares can be in no better condition than the assignor. . . . The question is simply whether the stock has been really paid in full to the corporation. The assignee may have paid for it to the assignors, and may have relied on the representations of the latter, and of officers of the company, that the shares bought were fully paid; yet creditors are not bound thereby, and if the stock was not fully paid, the holder is liable to creditors for the amount remaining unpaid." This case must be considered poor law.

⁴ Erskine v. Loewenstein, 11 Mo. App. 595 (1884).

deemed "paid up" in his hands, and he is protected as a *bona fide* purchaser, even though there is nothing on the face of the certificate stating that they are paid up.¹ This can hardly be said to be the established rule.² Yet it is based on sound public policy, favoring, as it does, the transfer of personal property, and the *quasi* negotiability of stock, and discountenancing secret liens and constructive notice. A purchaser in open market of stock represented to be paid up by a statement to that effect on the certificate, is presumed to be a *bona fide* purchaser. Hence, there has arisen the well established rule, both in America and England, that a *bona fide* purchaser for value, and without notice, of stock issued as paid up, is not liable for any part of the par value which may not have been paid.³

¹ *Keystone Bridge Co. v. McCheney*, 8 Mo. App. 496 (1880); *Foreman v. Bigelow*, 4 Cliff. 508 (1878), as explained in 8 Mo. App. 496; *Johnson v. Sullivan*, 15 Mo. App. 55 (1884), where the court says: "If any presumption of fact arises from the face of a stock certificate in customary form, as was the one in this case, it is that the stock . . . is fully paid up." See also *Erskine v. Loewenstein*, 82 Mo. 301 (1884).

² *Burkinshaw v. Nicolls*, L. R., 3 App. Cas. 1004-1017 (1878). In *Brant v. Ehlen*, 59 Md. 1 (1882), the court says: "The purchaser is not bound to suspect fraud, when everything seems fair. . . Any other doctrine would virtually destroy the transferable nature of such shares, and paralyze the whole of the dealings in the stock of the corporations."

³ In *Re British Farmers Pure Linseed Cake Co.*, L. R., 7 Ch. D. 533 (1880); *aff'd* L. R. 3 App. Cas. 1004 (1878), the court held that if the *bona fide* purchaser were not protected "no person buying shares in the market, as paid up shares, would be safe, for he would get nothing more than a certificate to show they are paid up. . . Obviously such a construction would destroy the transferable nature of shares altogether." See also *Foreman v. Bigelow*, 4 Cliff. 508 (1878); *McCracken v. McIntyre*, 1 Duv. (Can.) 479; *Stacey v. Little Rock & Ft. S. R. Co.*, 5 Dill. 348 (1878); *Jackson v. Sligo, &c., Co.*, 1 Lea (Tenn.), 210; *Brant v. Ehlen*, 59 Md. 1 (1883); *Waterhouse v. Jamieson*, L. R., 2 H. L. (Sc.) 29; *cf.* *Crickmer's Case*, L. R., 10 Ch. App. 614. *Contra*, *Myers v. Seeley*, 10 Natl. Bank

Reg. 411. It is immaterial that the payment in stock issued as paid up turns out to have been valueless. The *bona fide* purchaser is protected and the corporation must allow registry by him. *Protection Life Ins. Co. v. Osgood*, 93 Ill. 69 (1879). In the case of *Wintringham v. Rosenthal*, 25 Hun, 580 (1881), the court held that a *bona fide* purchaser of stock, which he purchased supposing it to be paid up, is not liable for the unpaid par value. The stock was issued by a bank, evidently on a cash subscription. Practically overruling *Mann v. Currie*, 2 Barb. 294 (1848). The general railroad act of New York (Laws 1850, ch. 140, § 10), prescribes that each stockholder shall be liable "to an amount equal to the amount unpaid on the stock held by him." In the case of *Tasker v. Wallace*, 6 Daly, 364-374 (1876), the court held that under this statute, "as between a stockholder and a creditor, it is wholly immaterial whether he was a *bona fide* and innocent purchaser of stock which the vendor assured him had been paid." This remark was, it seems, a *dictum*, and being by an inferior court, is doubtful as an authority. The representation, moreover, was not on the face of the certificate, nor was it made by the corporation. In the case of *Hubbell v. Meigs*, 50 N. Y. 480-489 (1872), where the purchaser of Wisconsin railroad stock, sued his vendor for damages for deceit on the ground, among others, that the stock had been issued fictitiously as paid up, the court said: "It is unnecessary to determine whether the corporation was authorized by its charter to sell its stock at less than par, or whether, in so selling, its officers did not violate their

Where a subscriber who has not yet taken out his certificate of stock instructs the corporation to issue the certificates to a designated transferee, the latter is held to be the original allottee of that stock, and if the stock was irregularly issued as paid up stock, he cannot claim to be a *bona fide* transferee without notice.¹

§ 51. *Third method issued by stock dividends.*—The third method of issuing fictitiously paid up stock is by a wrongful use of the power to issue stock dividends. It seems to be generally conceded that if the capital stock and the actual property of the corporation is not permanently increased to the extent of the par value of the stock distributed as a dividend, then that the issue of stock by such dividend is irregular, and under certain circumstances fraudulent.² In some of the States stock dividends are prohibited by constitutional or statutory provisions.³

duty. The plaintiff was a *bona fide* purchaser, and being such, acquired a valid title to the stock transferred to him."

¹ Rowland's Case, 42 L. T., N. S., 785 (1880); Potter's Appeal, Weekly Notes, 1878, p. 81; *Re Vulcan Iron Works*, Law Times, 1885, p. 61. A contrary doctrine is laid down in Carling's Case, L. R., 1 Ch. D. 115 (1875).

² In *Williams v. Western Union Tel. Co.*, 93 N. Y. 189 (1883), the court said that a stock dividend "could be declared by a corporation without violating its letter, its spirit, or its purpose. . . . There is no public policy which, in all cases, condemns such dividends. . . . No harm is done to any person, provided the dividend is not a mere inflation of the stock of the company, with no corresponding values to answer to the stock distributed. . . . So long as every dollar of stock issued by a corporation is represented by a dollar of property, no harm can result to individuals or the public from distributing the stock to the stockholders." *Howell v. Chicago & Northw. R'way Co.*, 51 Barb. 378 (1868), is to the same effect. In *Bailey v. Railroad Co.*, 22 Wall. 604, the court said that net earnings, however expended or invested, "belongs to the stockholders, and may be distributed as they may direct, in dividends of stock or by a sale of property." See also Chapter on Dividends.

³ Ill. Con., Art. XI, § 18. In Wisconsin by Statute. R. S., 1878, § 1753;

am'd by ch. 93, Laws 1881. So in Massachusetts. Pub. Stat., ch. 112, § 61. In one point of view a stock dividend is objectionable. They are issued to represent the increased value of the corporate property as it stands. In the case of railroads this increase of value arises very largely from the increased value of the eminent domain franchises which the corporation is using. These franchises belong to the people, and the people are entitled to the increased value of them. Such an increased value could be readily secured to the people by a reduction of railroad charges. But by stock dividends based on this increased value of the franchise, the railroad is able, by increasing its stock, to divide all profits and yet not declare more than a six or eight per cent. dividend. The smallness of the dividend prevents a legislative reduction of rates. If, however, no stock dividend were allowed, and the increased earning capacity of the railroad gave large profits, such profits would have to be employed in improving the property or in making extravagant dividends which would justify a reduction of railroad rates. It is urged, in reply to this view, that about three out of four of railroad enterprises are the cause of total loss to their projectors, and that the fourth should be made to pay more largely, by reason of the risk incurred; also that large capital and great ability in managing enterprise of such magnitude should be more fully compensated.

CHAPTER IV.

THE FORMATION OF THE CONTRACT OF SUBSCRIPTION.

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| <p>§ 52-54. Generally no formalities necessary.</p> <p>55-56. Cases in which the subscriber was held not bound by reason of irregularity or informality.</p> <p>57. The English rule.</p> <p>58. Statutory rules as to the formation of the contract of subscription.</p> <p>59. Subscriptions to commissioners.</p> <p>60. Who is competent to subscribe for stock. — Corporations generally not.</p> <p>61. Commissioners, directors, partners, &c., as subscribers.</p> <p>62. Married women as subscribers.</p> <p>63. Infant as subscriber.</p> <p>64. Agent as subscriber.</p> <p>65. Subscriptions made by an unauthorized agent of the subscriber.</p> | <p>§ 66. Subscriptions taken by an unauthorized agent of the corporation.</p> <p>67. Agreements to subscribe made before organization.</p> <p>68. In New England an express promise necessary.</p> <p>69. A subscription for shares is an implied promise to pay for them.</p> <p>70. Consideration for such agreements.</p> <p>71. Subscriptions delivered in escrow.</p> <p>72. Subscriptions in excess of the capital stock.</p> <p>73. Proof of subscription.</p> <p>74. Liability of the corporation for refusal to issue stock.</p> <p>75. Substitution of stockholders before the issue of the stock.</p> <p>76. Right to recover back money advanced on shares upon a failure to organize the company.</p> |
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§ 52. *Generally no formalities necessary.*—The contract of subscription for shares of stock in an incorporated company may be entered into in various ways. Whenever an intent to become a subscriber is manifested, the courts incline, without particular reference to formality, to hold that the contract of subscription subsists. It is, as in the case of other contracts, very much a question of intent. Accordingly, formal rules are for the most part disregarded, and whenever it is shown that a person intended to subscribe, and manifested such intention by some express or overt act, the court will usually hold the person a subscriber. Mere irregularity of form, or informalities in the manner of the subscription, will not, as a rule, operate to release a subscriber.¹ In general a contract of subscription may be made in any way in which other similar contracts may be lawfully made.²

Any agreement by which a person shows an intention to be-

¹ Mexican Gulf, &c., R. R. Co. v. Vivant, 6 Rob. (La.) 305 (1843); Boston, &c., R. R. Co. v. Wellington, 113 Mass. 79 (1873); Fry v. Lexington, &c., R. R. Co. 2 Metc. (Ky.) 314 (1859); Oakes v. Turquand, L. R. 2 H. of L. 325 (1867).

² Its validity commonly depends upon the law of the State creating the corporation, unless payment is to be made elsewhere. Penobscot, &c., Co. v. Bartlett, 78 Mass. 244 (1858).

come a stockholder is sufficient to bind both him and the corporation.¹ Where one accepts, or assumes, the position and duties, and claims the rights and privileges and emoluments of a stockholder, and the corporation accepts or acquiesces therein, such person is estopped to deny that he is bound thereby and subject to the obligations of a subscriber, although there may have been something irregular, or defective, in the form or manner of his subscription, or even if there have been no subscription.² In the absence of a formal subscription, a mere promise to subscribe for a certain amount of stock in a corporation for the purpose of inducing the selection of a particular route for a road has been

¹ *Wellsburg, &c., Co. v. Young*, 12 Md. 476 (1858); *Dutchess, &c., Co. v. Mobbett*, 58 N. Y. 397 (1874); *Blunt v. Walker*, 11 Wis. 334 (1860); *Gill v. Kentucky, &c., Co.* 7 Bush, 635 (1870); *Oler v. Baltimore, &c., R. R. Co.* 41 Md. 583 (1874); *Schaeffer v. Missouri, &c., Co.* 46 Mo. 248 (1870); *Fry v. Lexington, &c., R. R. Co.* 2 Metc. (Ky.) 314 (1859).

² *Sanger v. Upton*, 91 U. S. 56 (1875); *Upton v. Tribilcock*, 91 Id. 45 (1875); *Wheeler v. Millar*, 90 N. Y., 353 (1882); *Hamilton, &c., Co. v. Rice*, 7 Barb. 159 (1849); *Dorris v. French*, 4 Hun, 292 (1875); *Sheffield, &c., Co. v. Woodcock*, 7 Me. & W. 574; *Ex parte Besley*, 2 Mac. & G. 176 (1850); *Burnes v. Pennell*, 2 H. of L. Cas. 497 (1849); *Clark v. Farington*, 11 Wis. 306 (1860); *Jewell v. Rock River, &c., Co.*, 101 Ill. 57 (1881); *Haynes v. Brown*, 36 N. H. 545 (1858); *Chaffin v. Cummings*, 37 Me. 76 (1853); *Chester, &c., Co. v. Dewey*, 16 Mass. 94 (1819); *Chase v. Merrimack Bank*, 36 Id. 564 (1837); *Griswold v. Seligman*, 72 Mo. 110 (1880); *Boggs v. Olcott*, 40 Ill. 303 (1866); *Musgrave v. Morrison*, 54 Md. 161 (1880); *South Bay, &c., Co. v. Gray*, 30 Me. 547 (1849); *Phœnix, &c., Co. v. Badger*, 67 N. Y. 294 (1876); s. c. 6 Hun, 293 (1875); *Palmer v. Lawrence*, 3 Sandf. 161 (1849); *Fisher v. Seligman*, 75 Mo. 13 (1881); *Phila., &c., R. R. Co. v. Cowell*, 28 Penn. St. 329 (1857); *Gouthwaite's Case*, 3 De G. & Sm. 258 (1850); *Burlinson's Case*, 3 Id. 18 (1849); *Cheltenham, &c., Ry. Co. v. Daniel*, 2 Q. B. 781; *Straffon's Case*, 1 De G., M. & G. 576 (1852); *Maguire's Case*, 3 De G. & Sm. 31 (1849); *Harward's Case*, L. R. 13 Eq. 30 (1871); *Hoare's Case*, 2 John. & H. 229 (1862); *Cromford, &c., Ry. Co. v. Lacey*, 3 Younge & J., 80 (1829). And see the dissenting opinion of Lord St. Leonards in *Spack-*

man v. Evans, L. R. 3 H. of L. Cas. 171, 197 (1868); *Harrison v. Heathorn*, 6 Man. & G. 81 (1843).

Where a director is required to be a stockholder, the act of serving as a director is an implied subscription for stock to the amount required in order to be a director. See *Pearson's Case*, L. R. 5 Ch. Div. 336; *McCoy's Case*, L. R. 2 Ch. Div. 1; *Hay's Case*, L. R. 10 Ch. 593-604; *Luke's Case*, L. R. 6 Ch. 469; *Harward's Case*, L. R. 13 Eq. 30; *Stephenson's Case*, 45 L. J. (Ch.) 488; *De Ruigne's Case*, L. R. 5 Ch. Div. 306-322; *Re Englefield Colliery Co. L. R. 8 Ch. Div. 388*.

Where, however, the names of certain persons were published as members of a board of directors of a banking corporation, with their knowledge, but without any act of assent on their part, and without either of them owning any stock in the bank, or participating in any way in the management of its affairs, it was held, after the failure of the bank, that the creditors had no right of action against them, inasmuch as they had done nothing actively to lead the creditors to believe that they were directors. *Hume v. Commercial Bank*, 9 Lea, 728 (1882); cf. *McHose v. Wheeler*, 45 Penn. St. 32 (1868). *Contra*, *Thompson v. Reno Savings Bank*, 10 Am. & Eng. Corp. Cases, 203 (Nev. 1885).

The certificate is no necessary part of the contract, and it is by no means essential that one be issued in order to make the contract of subscription valid and binding. *Hawley v. Upton*, 102 U. S. 314 (1880); *Buffalo, &c., R. R. Co. v. Dudley*, 14 N. Y. 336, 347 (1856); *New Albany, &c., R. R. Co. v. McCormick*, 10 Ind. 499 (1858); s. c. 71 Am. Dec. 337 (note); *Mitchell v. Beckman*, 64 Cal. 117; *Agricultural Bank v. Wilson*, 24 Me. 273.

held valid, if accepted by the company, and enforceable against the promisor,¹ and it has been elsewhere held—and it is the better rule—that a mere informal subscription or promise to take stock, prior to the signing of the articles of association has, standing alone, no legal validity.² The question whether, in a given state of circumstances, the defendant intended to subscribe, is for the jury.³

It has been held that a contract of subscription must be in writing, and that it cannot be entered into by parol.⁴ Doubtless this is the rule where, by a statute, or by the act of incorporation, any particular form for the contract of subscription is prescribed. If a form of subscription is authorized, and particularly if it is expressly required that the contract be in writing, a substantial compliance with the rule declared, and the signature of the subscriber will be held necessary to the validity of the undertaking. Without the substantial compliance, and the written

¹ *Rhey v. Evensburg, &c., Co.*, 27 Penn. St. 261 (1856); *West Cornwall, &c., Ry. Co. v. Mowatt*, 15 Q. B. 521 (1850). *Cf. Drover v. Evans*, 59 Ind. 454.

² *New Brunswick, &c., Co. v. Muggeridge*, 4 Hurl. & N. 160 (1859); *Troy, &c., R. R. Co. v. Tibbits*, 18 Barb. 297 (1854); *Troy, &c., R. R. Co. v. Warren*, 18 Id. 310 (1854); *Clark v. Continental, &c., Co.*, 57 Ind. 135; *Thrasher v. Pike Co. R. R. Co.*, 25 Ill. 393 (1861); *Charlotte, &c., R. R. Co. v. Blakely*, 3 Strobb., 245 (1848); *McClelland v. Whiteley*, 11 Biss. 444 (1883); *Tilsonburg, &c., Co. v. Goodrich*, 8 Ontario (Q. B. Div.), 565.

³ *Galveston, &c., Co. v. Bolton*, 46 Texas, 633 (1877); *Phila., &c., R. R. Co. v. Cowell*, 28 Penn. St. 329 (1851). In an old case in Massachusetts it was held that a declamatory statement, at a public meeting of the corporation, by one of the stockholders, that he would spend half his estate, or enough of it to make the enterprise undertaken by the corporation a success, did not render him liable for a failure to do so. *Andover, &c., Co. v. Hay*, 7 Mass. 102 (1810).

But where an actual subscription is made, with a view to influencing other subscriptions, but the number of shares to be taken is left blank, so that the subscription itself might be subsequently withdrawn, it was held that the corporate agents might fill up the blank, and thereby bind the subscriber. *Jewell v. Rock River, &c., Co.*, 101 Ill. 57 (1881).

And where one took a book for subscriptions from an agent of the corporation, and subscribed himself and persuaded others to subscribe, and kept the book some months, but finally, because of a difference with the agent about the payment for his services, cut his name out of the book and returned it to the company, it was held, in an action by the company for the amount of his subscription, that he was bound thereon just as though he had left his name on the list of subscribers. *Greer v. Chartiers R. R. Co.*, 96 Penn. St. 391 (1880). See also *Railroad Co. v. White*, 10 S. C. 155 (1878).

It has been held however, in New York, that where the statutory certificate required by law to be filed in order to obtain incorporation remains in the hands of a subscriber, or either of them, a subscriber may erase or modify his subscription as he sees fit, even though he had, previously, induced others to subscribe. *Burt v. Farrar*, 24 Barb. 518 (1857).

⁴ *Pittsburgh, &c., R. R. Co. v. Gazam*, 32 Penn. St. 340 (1858); *Vreeland v. New Jersey, &c., Co.*, 29 N. J. Eq. 188 (1878); *Thames, &c., Co. v. Sheldon, & Barn. & C.* 341 (1827); *Fanning v. Insurance Co.* 37 Ohio St. 339 (1881); *Galveston, &c., Co. v. Bolton*, 46 Texas, 633 (1877); *Brown v. Appleby, & Sandf.* 170 (1847). See also *Phoenix, &c., Co. v. Badger*, 67 N. Y. 294 (1876).

subscription, the contract is invalid.¹ But, as already stated, the contract of subscription may arise, without an express agreement, either oral or written. The acts of the parties are by themselves sufficient to constitute one a subscriber for stock. This rule is based on estoppel and a wise public policy. It often is necessary, also, to protect corporate creditors.

§ 53. A subscription in a small pocket memorandum book has been held sufficient to bind the subscriber. No proof of the transfer of such a subscription to the corporate records, nor of its acceptance by the corporation is necessary.² So, a subscription on a single sheet of paper may be binding,³ even though the charter provides for the opening of books.⁴ A signature to the certificate required by statute to be filed in order to obtain the charter of incorporation, with the number of shares placed opposite to the signature, is a sufficient subscription to bind both the corporation and the subscriber.⁵ Where duplicate sets of articles are used for the purpose of obtaining subscriptions, and one set, signed by several persons, and accompanied by the proper affidavit, is filed in the office of the secretary of State, while the other set, subscribed by different individuals, is not so filed, the subscribers to the latter paper have been held not to become members of the corporation, and are not liable upon their subscriptions;⁶ but it is doubtful whether this is good law.

§ 54. The contract of subscription may also be entered into, and a liability thereon created, by merely accepting and holding

¹ See, in addition to the three cases last cited, *Dutchess, &c., R. R. Co. v. Mabbett*, 58 N. Y. 397 (1874); *Carlisle v. Saginaw, &c., R. R. Co.* 27 Mich. 315 (1873); *Fanning v. Insurance Co.* 37 Ohio St. 328 (1881); *Troy, &c. R. R. Co. v. Tibbits*, 18 Barb. 297 (1854); *Troy, &c., R. R. Co. v. Warren*, 18 Id. 310 (1854).

² *Buffalo, &c., R. R. Co. v. Gifford*, 87 N. Y. 294 (1882); *Brownlee v. Ohio, &c., R. R. Co.*, 18 Ind. 68 (1862). But see *McClelland v. Whiteley*, 11 Biss. 444 (1883).

³ *Iowa, &c., R. R. Co. v. Perkins*, 28 Iowa, 281 (1869); *Hamilton, &c., v. Rice*, 7 Barb. 157 (1849). *Cf. Bucher v. Dillsburg, &c., R. R. Co.*, 76 Penn. St. 306 (1874); *Hawley v. Upton*, 102 U. S. 314 (1880).

⁴ *Mexican Gulf, &c., R. R. Co. v. Viavant*, 6 Rob. (La.) 305 (1843); *Ashtabula, &c., R. R. Co. v. Smith*, 15 Ohio St. 328 (1864).

⁵ *Phoenix, &c., Co. v. Badger*, 67 N. Y. 294 (1876); s. c. 6 Hun, 295; *Nulton v. Clayton*, 54 Iowa, 425 (1880).

⁶ *Erie, &c., R. R. Co. v. Owen*, 32 Barb. 616 (1860). In this case it is said that there are two modes in which a person, under the general railroad act of the State of New York, may become a stockholder in a railroad corporation, viz., by subscribing the articles of association, and becoming a member of the corporation as the act provides (§§ 1 and 2), or by subscribing to the capital stock, in the book opened by the directors, after the corporation is in existence, and that no one who has only signed the articles of association, before the corporation came into being, is a corporator or member of the corporation, unless the articles so signed by him have been duly filed in the office of the secretary of State, as required by the statute.

a certificate of stock.¹ And it is also the rule that an acceptance of a certificate of stock is a waiver of all informalities, or irregularities as to the subscription, except a defect of jurisdiction.² So where the name of an individual appears upon the stock book of a corporation as a stockholder, the presumption is that he is regularly and lawfully the holder and owner of the stock, and, in the absence of evidence that the stock has come to him by transfer, that he was regularly a subscriber.³ Immaterial irregularities or defects in the subscription paper will not avail to avoid the subscription, as, for example, where a subscription paper does not correctly designate the termini of a railroad already built.⁴ And while on the one hand the legislature has no power to constitute one a member of a private corporation without his consent, or in opposition to his wishes,⁵ it may, on the other hand, cure, by amendment of the charter or otherwise, mere irregularities with respect to the subscriptions, so that the subscribers cannot take advantage of them subsequently.⁶

§ 55. *Cases in which, by reason of irregularity or informality, the subscriber has been held not bound.*—While it is the conceded tendency of the law to look rather to the intent of the parties than to the form of the subscription, and to overlook and disregard mere irregularities and informalities, still there are

¹ *Upton v. Tribilcock*, 91 U. S. 45 (1875); *McLoughlin v. Detroit, &c., R. R. Co.*, 8 Mich. 100 (1860); *In re South Mountain, &c., Co.*, 7 Sawyer, 30 (1881). *Cf. McHose v. Wheeler*, 45 Penn. St. 32 (1863). See also *Clarke v. Continental, &c., Co.*, 57 Ind. 135, 138.

² *Hamilton, &c., Co. v. Rice*, 7 Barb. 157 (1849); *Lone v. Brainerd*, 30 Conn. 565 (1862).

³ *Pittsburgh, &c., R. R. Co. v. Applegate*, 21 West Va. 172 (1882); *Turnbull v. Payson*, 95 U. S. 418 (1877); *Hoare's Case*, 2 John. & H. 229 (1862); *Taylor v. Hughes*, 2 Jones & Lat. (Irish Chan.) 24, 55 (1844); *McHose v. Wheeler*, 45 Penn. St. 32 (1863).

⁴ *Boston, &c., R. R. Co. v. Wellington*, 113 Mass. 79 (1873); *Cayuga, &c., R. R. Co. v. Kyle*, 64 N. Y. 185 (1876). See also *Phoenix, &c., Co. v. Badger*, 67 Id. 294 (1876); *Burlington, &c., R. R. Co. v. Palmer*, 42 Iowa, 222 (1875); *Clark v. Continental, &c., Co.*, 57 Ind. 135.

⁵ *Richmond, &c., Co. v. Clarke*, 61 Me. 351 (1873).

⁶ *Rice v. Rock Island, &c., R. R. Co.*, 21 Ill. 93. In *The Thames Tunnel Company v. Sheldon*, 6 Barn. & C. 341 (1827), Bayley, J., held that the word "subscriber," in this connection, is to be applied to those only who have stipulated that they will make payment, and not to those who have already advanced money, and consequently, that one whose name is mentioned in an act of parliament as one of the original proprietors and who has paid a deposit on certain shares, but has not signed any contract, is not a "subscriber," and not liable to be sued by the directors. In the opinion in this case the word is elaborately defined, and it is held to mean only such persons as have entered into an express contract to take up a certain definite number of shares. See, also, a definition at some length by Cooley, J., in *Peninsular, &c., R. R. Co. v. Duncan*, 28 Mich. 130 (1878). *Cf. Franklin Glass Co. v. Alexander*, 2 N. H. 380 (1849); s. c. 9 Am. Dec. 92, and the note, 96-104; *Hartford, &c., R. R. Co. v. Kennedy*, 12 Conn. 500 (1838).

many cases in which informalities and irregularities as to the form or substance of a subscription have been held sufficient to destroy the validity of the undertaking, and to release the subscriber from his obligation thereunder. Thus a subscription to an incomplete copy of the articles of association will not bind the subscriber¹; and where articles are materially altered without the consent of all the subscribers, after their subscription and before the complete organization of the company, such articles are not binding upon the non-consenting subscribers.² Again, a subscription paper in which the names of directors were left blank has been held not enforceable against a subscriber after the blank has been filled without his consent or concurrence.³ Equity will not, however, in the absence of fraud, relieve a subscriber merely upon the ground that he by mistake subscribed for more stock than he intended, in a case where he suffered the corporation to act upon the faith of his subscription.⁴ But if one signs an agreement to subscribe, on a subscription paper, entirely misunderstanding the nature of the contract he is entering into, his subscription must, on general principles, be treated as null and void for want of mutual consent. Cases of this nature may arise without involving the question of fraud.⁵

¹ *Dutchess, &c., R. R. Co. v. Mabbett*, 58 N. Y. 397 (1874); *Bucher v. Dillsburg, &c., R. R. Co.*, 76 Penn. St. 306.

² *Burrows v. Smith*, 10 N. Y. 550 (1853); *Tilsonburg, &c. Co. v. Goodrich*, 8 Ontario (Q. B. Div.) 565 (1885). See also *Eakright v. Logansport, &c. R. R. Co.*, 13 Ind. 404 (1859); and compare *Reed v. Richmond, &c., R. R. Co.*, 50 Ind. 342 (1875); *Kansas, &c. R. R. Co. v. Hunt*, 57 Mo. 126 (1874).

³ *Dutchess, &c. R. R. Co. v. Mabbett*, 58 N. Y. 397 (1874), the court saying: "A signature to an incomplete paper, wanting in any substantial particular, when no delegation of authority is conferred to supply the defect, does not bind the signer without further assent on his part to the completion of the instrument." To same effect, *Consol's Ins. Co. v. Newall*, 3 Foster & F. 130 (1862), where the number of shares was left in blank. In the case of a subscription after organization it has been held that the subscriber does not become a stockholder until the company has issued a certificate to him, or in some other proper manner recognized him as a member. *Sewall v. East-*

ern R. R. Co., 9 Cush. 5 (1851); *Carlisle v. Saginaw, &c. R. R. Co.*, 27 Mich. 315 (1873); *Parker v. Northern, &c. R. R. Co.*, 33 Id. 23 (1875); *St. Paul, &c. R. R. Co. v. Robbins*, 23 Minn. 439 (1877); *Clark v. Continental, &c. Co.*, 57 Ind. 135. *Of. Thrasher v. Pike Co. R. R. Co.*, 25 Ill. 393 (1861). The case of *Clark v. Continental, &c. Co.*, 57 Ind. 134, held that an agreement to pay in instalments a certain sum to a contractor as the work progresses, in consideration of stocks to be delivered by the corporation, after full payment has been made in this way, was not a subscription to capital stock, and that the maker of such an agreement was not a subscriber.

⁴ *Diman v. Providence, &c. R. R. Co.*, 5 R. I. 130 (1858).

⁵ *County of Schuylkill v. Copley*, 67 Penn. St. 386 (1871); *Jackson v. Hayner*, 12 Johns. 469 (1815); *Smith v. Reese, &c. Co.*, L. R. 2 Eq. 264 (1866). *Of. Throughgood's Case*, 2 Rep. 9; *Foster v. Mackinnon*, L. R. 4 C. P. 704 (1869); *Rockford, &c. R. R. Co. v. Schunick*, 65 Ill. 223 (1872).

§ 56. A subscriber to the capital stock of an incorporated company is, in general, bound to know the legal effect of his subscription,¹ and false and even fraudulent representations made to him at the time of taking his subscription, as to the legal effect of his contract of subscription, are not sufficient to release him. This doctrine has been well established by the Supreme Court of Indiana.² A defendant, it is said, however, who is sued on a subscription absolute, may show that he agreed orally to subscribe conditionally, and placed his name on blank paper, and that the secretary of the corporation subsequently, without his knowledge, subscribed the name unconditionally to a subscription paper.³ And it is held that when a corporation invites and accepts subscriptions as a loan, to be repaid in full and the subscription cancelled, it cannot repudiate such a contract and treat the subscription so induced as absolute.⁴ But where the corporation contracts with the subscriber to give him indefinite time in which to pay for his stock, the subscription is void.⁵ It is otherwise when only a reasonable credit is given.⁶ It has been held that a subscription may be withdrawn at any time before the filing of the articles of incorporation⁷; but the better rule is that when a sub-

¹ *Ellison v. Mobile, &c., R. R. Co.*, 36 Miss. 572 (1858); *Wight v. Shelby R. R. Co.*, 16 B. Mon. 4 (1855); *Selma, &c. R. R. Co. v. Anderson*, 51 Miss. 829, 833 (1876); *Smith v. Reese, &c. Co.*, L. R. 2 Eq. 264 (1866). See also *Bailey v. Hannibal, &c., R. R. Co.*, 17 Wall. 96 (1872). *Cf. Vicksburg, &c., R. R. Co. v. McKean*, 12 La. Ann. 638 (1857).

² *Clem v. Newcastle, &c. R. R. Co.*, 9 Ind. 488 (1857); *New Albany, &c. R. R. Co. v. Fields*, 10 Id. 187 (1858); *Thornburgh v. New Castle, &c. R. R. Co.*, 14 Id. 499 (1860). "The contract of subscription," said the High Court of Errors and Appeals of Mississippi, in speaking to the point, "necessarily had reference to the charter of the company, which was the great law both of the liability and of the rights of the stockholder. He must be held to have subscribed for stock, subject to the rules therein declared and to the powers therein expressly granted or necessarily implied; and no consideration can be permitted to enter into and form a part of the contract of subscription which is incompatible with the powers granted in the charter, or which may be

prejudicially affected by the exercise of the legitimate powers and duties appertaining to the company under its charter. So far as the nature and obligation of his contract are defined and secured by express stipulation in the charter, he has the right to insist upon the strict law as forming the basis of his contract; but when, from the nature of the provisions of the charter, a general power is conferred upon the company, the exercise of which may operate to his inconvenience or disadvantage, he is to be presumed to have contracted with that view, and must submit to its operation." *Ellison v. Mobile, &c. R. R. Co.*, 36 Miss. 572, 588 (1858).

³ *Tonica, &c. R. R. Co. v. Stein*, 21 Ill. 96 (1859). *Cf. Bucher v. Dillsburg, &c. R. R. Co.*, 76 Penn. St. 306 (1874); *Brewers, &c. Ins. Co. v. Burger*, 10 Hun, 56 (1877).

⁴ *Nellis v. Coleman*, 98 Penn. St. 465 (1881).

⁵ *McComb v. Credit Mobilier, &c. Co.*, 13 Phila. 468; *Van Allen v. Illinois, &c. R. R. Co.*, 7 Bosw. 515 (1861).

⁶ *Mitchell v. Beckman*, 64 Cal. 117.

⁷ *Garrett v. Dillsburg, &c. R. R. Co.*, 78 Penn. St. 465 (1875); *Holt v. Winfield*

scription is made with full knowledge of the scope and purpose of the undertaking, in the absence of fraud, it is, especially when it has been acted upon either by the corporation or the other subscribers, irrevocable and absolutely binding upon the subscriber.¹

§ 57. *The English rule.*—In England the contract of subscription for shares is entered into in a somewhat more technical or formal manner. An application, in the first instance, is made in writing for a specified number of shares, which application is held to be a mere offer, open for acceptance by the corporation for only a limited time.² If the application be accepted, the corporation formally allots to the applicant the desired number of shares, and gives him a notice of the allotment. The notice is of the essence of the contract. An allotment without notice is not sufficient to bind the applicant as a contributory or a shareholder.³ If the notice of allotment is sent by mail, the allottee becomes bound from the time of posting the letter, whether he received it or

Bk., 25 Fed. Rep. 812 (1885); *Cook v. Chittenden Bk.*, 25 Fed. Rep. 544 (1885), allowing a withdrawal where no others have subscribed in reliance thereon, nor creditors' debts incurred. *Gaff v. Flesher*, 33 O. St. 107 (1877); *Gulf C. & C. Ry. Co. v. Neely*, 64 Texas, 344 (1885), holding that there can be no withdrawal after an acceptance by the corporation. *Cf. Tiltonburg, & C. Co. v. Goodrich*, 8 Ontario (Q. B. Div.), 565 (1885); *Ross v. San Antonio, & C., R. R. Co.*, 31 Tex. 49 (1868); and see Chapter X on Defense of Cancellation of Subscription.

¹ *Hughes v. Antietam, & C. Co.*, 34 Md. 316 (1870); *Hutchins v. Smith*, 46 Barb. 235; *Kidwelly, & C. Co. v. Raby*, 2 Price (Exch.), 93 (1816); *New Albany, & C. R. Co. v. McCormick*, 10 Ind. 499 (1858). A line of cases may also be found in which it is held that acceptance by the corporation is essential to the validity of the contract, and that contracts of subscription become binding only when they have been accepted by the corporation. *New Albany, & C. R. Co. v. McCormick*, 10 Ind. 499 (1858); *Spear v. Crawford*, 14 Wend. 20 (1835); *Payne v. Bullard*, 23 Miss. 88 (1851); *Instone v. Frankford Bridge Co.*, 2 Bibb, 576 (1812); *Brownlee v. Ohio, & C. R. R. Co.*, 18 Ind. 72 (1862). *Cf. Cin-*

cinnati, & C. R. Co. v. Pearce, 28 Ind. 508 (1867); *Lincoln v. State*, 36 Id. 163 (1871); *Beaver v. Hartsville University*, 34 Id. 248 (1870); *Branham v. Record*, 42 Id. 198 (1873); *Slipher v. Earhart*, 83 Id. 178 (1882).

² *Ramsgate, & C. Co. v. Montefiore*, L. R. 1 Exch. 109 (1866); *In re Bowron*, L. R. 5 Eq. 428 (1868), and the cases generally cited, *infra*, in this section.

³ *Hebbs' Case*, L. R. 4 Eq. 9 (1867); *Gunn's Case*, L. R. 3 Chan. 40 (1867); *In re Peruvian Ry. Co.*, L. R. 4 Chan. 322 (1869); *Pellatt's Case*, L. R. 2 Chan. 527 (1867); *Ward's Case*, L. R. 10 Eq. 659 (1870); *Harris' Case*, L. R. 7 Chan. 587 (1872); *Household, & C. Co. v. Grant*, L. R. 4 Exch. Div. 216 (1879). The mere act of signing the memorandum of association does not make one a stockholder. *Mackley's Case*, L. R. 1 Ch. Div. 247 (1875). A mere allotment without an entry of the name on the stock registry does not render the person liable as a stockholder. *Nicoll's Case*, L. R. 29 Ch. Div. 421 (1883). Nor is one a stockholder unless he signs the deed of settlement. *Irish Peat Co. v. Phillips*, 1 Best & S. 598 (1861). Nor will a certificate be issued till then. *Wilkinson v. Anglo, & C. G. M. Co.*, 18 Q. B. 728 (1852).

not.¹ And if the allottee knew in fact of the allotment, and especially if he acted or suffered others to act upon the assumption that he was a shareholder, a formal notification may be unnecessary to bind him.² The application, being in the nature of an offer or a proposition, may be withdrawn at any time before it has been regularly accepted, and it must be accepted within a reasonable time, or the party making it cannot be held bound;³ and although the application should be in writing, the withdrawal of it may be oral.⁴ It seems to be well settled in England, that in order to make the contract to take up shares completely binding, there must be the application in writing, the allotment of the shares to the applicant, and a communication to him of notice of the allotment.⁵

§ 58. *Statutory rules as to the formation of the contract of subscription.*—Frequently, the manner of forming the contract of subscription in these cases is fixed by statute, but even then non-conformity with the statutory regulations will not necessarily vitiate the subscription.⁶ A substantial compliance, in good faith, with the provisions of the charter, or the act of incorporation regulating the matter of subscriptions, will suffice.⁷

¹ Harris' Case, L. R. 7 Chan. 587 (1872); Household, &c. Co. v. Grant, L. R. 4 Exch. Div. 216 (1879); Townsend's Case, L. R. 13 Eq. 148; Hebbs' Case, L. R. 4 Eq. 9 (1867). *Contra*, British, &c. Telegraph Co. v. Colson, L. R. 6 Exch. 108 (1871); *In re Constantinople, &c. Co.*, 19 W. R. 219 (1870).

² Levita's Case, L. R. 3 Chan. 36 (1867); *In re Peruvian Ry. Co.*, L. R. 4 Chan. 322 (1869); Richards v. Home, &c. Assoc., L. R. 6 C. P. 591 (1871); Pellatt's Case, L. R. 2 Chan. 527 (1867).

³ Ward's Case, L. R. 10 Eq. 659 (1870); Best's Case, 2 De G., J. & S. 650 (1865); Ramsgate, &c. Co. v. Montefiore, L. R. 1 Exch. 109 (1866); Chapman's Case, L. R. 2 Eq. 567 (1866); Ritso's Case, L. R. 4 Chan. Div. 774 (1877); Wilson's Case, 20 L. T. (N. S.) 962 (1869).

⁴ Wilson's Case, 20 L. T. (N. S.) 962 (1869).

⁵ Adam's Case, L. R. 13 Eq. 474; Hebbs' Case, L. R. 4 Eq. 9 (1867); Pellatt's Case, L. R. 2 Chan. 527 (1867); Roger's Case, L. R. 3 Chan. 637 (1868); Tucker's Case, 20 W. R. 89 (1871). *Cf.* Bloxam's Case, 33 Beav. 529, distinguished in Pellatt's Case, *supra*. But un-

der the 23d section of the Companies Act of 1862, the decisions are uniform that whenever one signs the memorandum of association he becomes a shareowner, and must be put on the list of contributories, although no shares may have been allotted to him. *In re London, &c. Co.*, L. R. 5 Chan. Div. 525 (1877); Evan's Case, L. R. 2 Chan. 427 (1867); Sidney's Case, L. R. 13 Eq. 228 (1871); Levick's Case, 40 L. J. (Chan.) 180 (1870); Hall's Case, L. R. 5 Chan. 707 (1870), distinguishing Snell's Case, L. R. 5 Chan. 22 (1869).

⁶ London, &c., Ry. Co. v. Fairclough, 2 Man. & G. 674 (1841); *Id.* v. Freeman, 2 Id. 606 (1841); Birmingham, &c., Ry. Co. v. Locke, 1 Q. B. 256 (1841); Wolverhampton, &c., Co. v. Hawksford, 11 C. B. (N. S.) 456 (1861); Gunn's Case, L. R., 3 Chan. 40 (1867); Peninsular, &c., R. R. Co. v. Duncan, 28 Mich. 130 (1873).

⁷ People v. Stockton, &c., R. R. Co., 45 Cal. 306 (1873); Ashtabula, &c., R. R. Co. v. Smith, 15 Ohio St. 328 (1864); Brownlee v. Ohio, &c., R. R. Co., 18 Ind. 68 (1862); Buffalo, &c., R. R. Co. v. Gifford, 87 N. Y. 294 (1882); Harris v. McGregor, 29 Cal. 124 (1865). So, for example, although the statute provides

§ 59. *Subscriptions to commissioners.*—But where the statute provides for subscription, either by an original subscription to the articles of association or, after the incorporation, by a subscription in books to be opened by commissioners, it has been held that a subscription in any other way, or to any other subscription paper, is not binding.¹ A better rule, however, is that a statute providing for subscriptions through commissioners does not necessarily invalidate subscriptions taken in some other way.² The commissioners may, *ex mero motu*, limit the amount of stock which any one subscriber may take, and will, in a proper case, be sustained therein on grounds of public policy, although the power so to act is not specifically conferred upon them by the statute.³ The commissioners may themselves be subscribers to the stock,⁴ but they can have no priority of right to subscribe over others, and no subscriptions can lawfully be taken with closed doors. The books must be open, and the public must have an opportunity to subscribe.⁵ The commissioners have only such general powers as are necessary to validate the subscriptions to the stock. Their authority and functions cease upon the organization of the corporation.⁶

for subscription books, yet a subscription on a subscription paper will be valid. *Hamilton, &c., Co. v. Rice*, 7 Barb. 157 (1849); *Stuart v. Valley R. R. Co.*, 32 Gratt. 146 (1879); *Mexican Gulf, &c., R. R. Co. v. Viavant*, 6 Rob. (La.) 305 (1843); *Woodruff v. McDonald*, 33 Ark. 97 (1878). Especially where the loose sheets are subsequently bound up into a volume and make part of the records of the corporation. *Woodruff v. McDonald*, 33 Ark. 97 (1878).

¹ *Troy, &c., R. R. Co. v. Tibbits*, 18 Barb. 297 (1854). See also *Parker v. Northern, &c., R. R. Co.*, 33 Mich. 23 (1875); *Unity Insurance Co. v. Cram*, 43 N. H. 636 (1862); *Field v. Cooks*, 16 La. Ann. 153 (1861).

² *Buffalo, &c., R. R. Co. v. Gifford*, 87 N. Y. 294 (1882); *Stuart v. Valley R. R. Co.*, 32 Gratt. 146 (1879). But when the statute provides for commissioners, it is said that they must all be present in order to the valid performance of the judicial duties assigned to them. *Crocker v. Crane*, 21 Wend. 211 (1839). It is said that in the taking of subscriptions, the commissioners act ministerially, but in the distribution or allotment of shares they act judicially, and that a distribu-

tion of shares by commissioners, not sufficient in number to constitute a legal board, is *coram non-judice* and void. *Crocker v. Crane*, *supra*.

³ *Brower v. Passenger R. R. Co.*, 3 Phila. 161 (1858). And accordingly fictitious subscriptions for the purpose of evading such a limitation of the amount of stock to be taken by a single subscriber, are illegal and void. *Perkins v. Savage*, 15 Wend. 412 (1836).

⁴ *Walker v. Devereaux*, 4 Paige, 229 (1833). See § 61.

⁵ *Brower v. Passenger Ry. Co.*, 3 Phila. 161 (1858). When the amount of the subscription is not limited, the commissioners, in the absence of other express provision, may usually decide when enough stock has been subscribed, and their decision is practically conclusive, as an exercise of discretion. *Saugatuck, &c., Co. v. Westport*, 39 Conn. 337, 348 (1872). Their failure to take the statutory oath will not invalidate the subscriptions taken by them, if they are in other essential respects regular. *Hollman v. Williamsport, &c., Co.*, 9 Gill & J. 462 (1838).

⁶ *James v. Cincinnati, &c., R. R. Co.*, 2 Disney (Cin. Super. Ct.), 261 (1868);

§ 60. *Who is competent to subscribe for stock.—Corporations generally not.*—Upon general common law principles, any one who is competent to enter into ordinary contracts may make a valid subscription for stock in an incorporated company. A subscription for stock properly made is a contract, and in general any one who can contract may subscribe. The corporation itself, however, cannot be a subscriber to its own stock.¹ It is conclusively settled that municipal corporations may lawfully subscribe for the stock of private corporations.² It is not equally clear that one private corporation may subscribe for the stock in another such corporation. On the contrary, such subscriptions are *ultra vires* and void, unless clearly within the ordinary objects and business of the subscribing corporation.³ A railroad corporation cannot subscribe for shares of stock in another railroad company;⁴ nor can a steamship company be held liable upon a subscription for stock in a dry dock company;⁵ nor can a manufacturing company legally invest its funds in the stock of a bank, for the pur-

Peninsular, &c., R. R. Co. v. Duncan, 28 Mich. 130 (1873); Hardenburgh v. Farmers, &c., Bank, 3 N. J. Eq. 68 (1834); Walker v. Devereaux, 4 Paige, 229 (1833); Crocker v. Crane, 21 Wend. 211 (1839); Wellersburg, &c., Co. v. Hoffman, 9 Md. 559 (1834); Smith v. Bangs, 15 Ill. 399 (1854); State v. Lehre, 7 Rich. Law, 234 (1854).

¹ Thus, where a number of individuals attempted to organize a corporation with a capital stock of 72,500 shares, of the par value of \$100 each, and six different persons subscribe for one share each, and one person then subscribes for the corporation as follows: "Oregon Central Railroad Company, by G. L. Wood, Chairman, seventy thousand shares, seven million dollars," it was held that this subscription was void, and that the corporation could not be created by such subscriptions. Holladay, v. Elliott, 8 Oregon, 84 (1879). And again it has been held that, where the directors of a company, in order to make up the required amount of capital stock, subscribed as trustees for the corporation itself, they are liable for calls on the amount so subscribed. But in the same case a bill by a member of the corporation on behalf of himself, and all the other members except the defendants, praying that this transaction, although it had been sanc-

tioned unanimously at a meeting of the company, might be declared fraudulent and void, was sustained, although some of the members, on behalf of whom the bill was filed, had been present and voted at that meeting. Preston v. Grand Colliery, &c., Co., 11 Sim. 327 (1840).

² Sharpless v. The Mayor, 21 Penn. St. 147 (1853), and the long train of decisions following. The matter of municipal subscriptions is fully considered in Chapter VI.

³ Thus, for example, a banking corporation cannot lawfully subscribe for stock in a railway corporation. Nassau Bank v. Jones, 95 N. Y. 115 (1884). Nor for stock in any other corporation, the business of which is wholly other than banking. Franklin Co. v. Lewiston Bank, 68 Me. 43 (1877); Mechanics' Bank v. Meriden Agency, 24 Conn. 159 (1855); Talmage v. Pell, 7 N. Y. 328 (1852). Cf. First National Bank v. National Exchange Bank, 92 U. S. 122 (1875); and see Royal Bank of India's Case, L. R., 4 Chan. 252 (1869); Joint Stock, &c., Co. v. Brown, L. R., 8 Eq. 381 (1869).

⁴ Maunsell v. Midland, Great Western Ry. Co., 1 Hem. & M. 130 (1863); and see Ch. XIX.

⁵ New Orleans, &c., Steamship Co. v. Dry Dock Co., 28 La. Ann. 173.

pose of carrying on the banking business.¹ All such contracts are in general *ultra vires* and void.²

§ 61. *Commissioners, directors, partners, &c., as subscribers.*—Commissioners, as we have seen,³ may be subscribers to the capital stock.⁴ So also may directors and corporate officers subscribe, and a director, in the absence of fraud or fraudulent intent, may subscribe for the whole of the unscribed stock, in his own name and for his own benefit.⁵ A partner, if the act be within the scope of the partnership business, may bind his firm by a subscription in the firm name.⁶ But if it is not within the scope of the partnership business, the person so signing is liable personally, and whether or not the subscription was within the scope of the partnership business is a question for the jury.⁷

§ 62. *Married women as subscribers.*—At common law, a married woman could not subscribe for stock, and any person subscribing in her name was himself personally liable on the subscription.⁸ But now, in England, and generally in the United States by statute, a married woman may bind her separate estate by such a subscription,⁹ and when it appears that the contract was plainly with the wife, having been made directly and solely with

¹ Sumner v. Marcy, 3 Woodb. & M. 106. See also Elysville, &c., Co. v. Okisko, &c., Co., 1 Md. Chan. 392 (1849), aff'd 5 Md. 152, where a railway company, without a special authority of law, assumed to purchase a steamboat to be run in connection with their road. The notes given for the purchase-money were held void by the Supreme Court of the United States, and the holder could not recover on them against the corporation. Pearce v. Madison, &c., R. R. Co., 21 How. 441 (1858). Cf. Central R. R., &c., Co. v. Smith, 76 Ala. 572 (1884); s. o. 52 Am. Rep. 353; Wheeler v. Santa Fe, &c., R. R. Co., 31 Cal. 46 (1866); Downing v. Mt. Washington R. R. Co., 40 N. H. 230 (1860).

² See Part IV.

³ § 59.

⁴ Walker v. Devereaux, 4 Paige, 229 (1833).

⁵ Sims v. Street Railroad Co., 37 Ohio St. 556 (1882); s. o. 4 Am. & Eng. R. R. Cases, 132 (1882). But neither the commissioners, Brower v. Passenger Ry. Co., 3 Phila. 161, nor any original stockholder,

Curry v. Scott, 54 Penn. St. 270 (1867), has any priority of right, in the absence of a statutory provision, over the other subscribers, or the public generally, in the matter of subscription for untaken stock. And a corporation may be held liable for improperly refusing, by its directors, to permit an individual to subscribe for its stock. Union Bank v. McDonough, 5 La. 63 (1833). Cf. Walker v. Mobile, &c., R. R. Co., 34 Miss. 245, 256 (1857).

⁶ Maltby v. Northwestern, &c., R. R. Co., 16 Md. 422 (1860); Ogdensburgh, &c., R. R. Co. v. Frost, 21 Barb. 541 (1856); Union Hotel Co. v. Hersee, 79 N. Y. 454 (1880).

⁷ Union Hotel Co. v. Hersee, *supra*.

⁸ Pugh & Sharman's Case, L. R., 13 Eq. 566 (1872); s. o. 41 L. J. (Chan.) 580.

⁹ Mrs. Matthewman's Case, L. R., 3 Eq. 781 (1866); Luard's Case, 1 De G., F. & J. 533 (1860); Pugh & Sharman's Case, *supra*; Butler v. Cumpston, L. R., 7 Eq. 16 (1868); In the Matter of the Reciprocity Bank, 22 N. Y. 9 (1860).

her, the husband is not bound.¹ The recourse of the corporation, or the corporate creditors is, in such a case, only to her separate estate.² In England, a husband has been held liable on his wife's subscription to the capital stock of an incorporated company, the subscription having been made before marriage.³

§ 63. *Infant as subscriber.*—A subscription for stock by an infant is a contract to be governed by the general rules of law that apply to the contracts of infants in respect of other similar matters. In general the contracts of infants, in matters of this nature, are voidable rather than void. The infant is not bound by the contract. He may repudiate it at majority, and thereby entirely escape liability, or he may ratify it, and thereby become as fully bound as though the subscription had been made after majority.⁴ Accordingly it is a settled rule, that where one subscribes for shares in the name of an infant, he is liable personally to the corporation or the corporate creditors on the subscription.⁵

The corporation may, moreover, refuse to receive an infant as a stockholder, even though, upon coming of age, he expresses his willingness to ratify and confirm the subscription or transfer, or the corporation may even repudiate his subscription, after accepting it, upon learning of the disability, unless they are estopped.⁶ An infant's subscription must be repudiated within a

¹ *Angas' Case*, 1 De G. & Sm. 560 (1849); *Dalton v. Midland, &c., Ry. Co.*, 13 C. B. 474 (1863); s. c. 22 L. J. (C. P.) 177; *Luard's Case*, *supra*.

² *Biggart v. City of Glasgow Bank*, 6 Rettie (Scotch Ct. of Sessions Cases), 470 (1879); *Mrs. Matthewman's Case*, L. R., 3 Eq. 781 (1866); *Ness v. Angas*, 3 Exch. 805 (1849).

³ *White's Case*, 3 De G. & Sm. 157 (1850); *Luard's Case*, 1 De G., F. & J. 533 (1860); *Burlinson's Case*, 3 De G. & Sm. 18 (1849); *Sadler's Case*, 3 Id. 36 (1849). *Cf. Kluht's Case*, 3 Id. 210 (1850). And also upon a legacy of stock to her during coverture, where it appeared that the stock had been transferred to her, and the transfer duly accepted by her and her husband, and that she only had signed the dividend warrants and drawn the dividends, the proceeds being applied to ordinary household expenses. *Thomas v. City of Glasgow Bank*, 6 Rettie (Scotch Ct. of Sessions Cases), 607 (1879).

⁴ *Lumsden's Case*, L. R., 4 Chan. 31

(1868); *Ebbett's Case*, L. R., 5 Chan. 302 (1870); *Baker's Case*, L. R., 7 Chan. 115 (1871); *Maguire's Case*, 3 De G. & Sm. 31 (1849); *Mitchell's Case*, L. R., 9 Eq. 363 (1870); *Wilson's Case*, L. R., 8 Eq. 240 (1869); *Hart's Case*, L. R., 6 Eq. 512 (1868).

⁵ This is upon the theory, it seems, that such a subscription is a fraud on the other subscribers and the creditors of the company. *Castleman v. Holmes*, 4 J. J. Marsh. 1; *Roman v. Fry*, 5 Id. 634; *Pugh & Sharman's Case*, L. R., 13 Eq. 566; s. v. 41 L. J. (Chan.) 580; *Weston's Case*, L. R., 5 Chan. 614; *Richardson's Case*, L. R., 19 Eq. 588; *Reaveley's Case*, 1 De G. & Sm. 550; *Ex parte Reaveley*, 1 Hall & Tw. 118; *Capper's Case*, L. R., 3 Chan. 458; *Castelo's Case*, L. R., 8 Eq. 504; *Symon's Case*, L. R., 5 Chan. 298. *Cf. Clements v. Bowes*, 1 Drew. 684; *Reid's Case*, 24 Beav. 318.

⁶ *Symon's Cases*, L. R., 5 Chan. 298; *Castelo's Case*, L. R., 8 Eq. 504. But see *Parson's Case*, L. R., 8 Eq. 656.

reasonable time after coming of age or he will be held to have ratified it.¹

§ 64. *Subscription by agent.*—A valid subscription may of course be made through an agent.² But a mere intent to subscribe, without an actual subscription, is not sufficient.³ Where one subscribes for stock in his own name, in pursuance of a verbal agreement between himself and another, that the stock should belong to them jointly, and that he should hold it on joint account, and the company subsequently becoming insolvent, the stockholders are called on to contribute an amount equal to their stock, it was held, in New York, that the nominal owner of the stock might have contribution from the joint owner.⁴

§ 65. *Subscriptions made by an unauthorized agent of the subscriber.*—No person can be made a subscriber to the capital stock of a corporation, and be subjected to the liabilities of a subscriber, by a subscription in his name, made by another without authority, but assuming to act as his agent. Such a subscription, so far as the person sought to be charged is concerned, is, in the absence of qualifying circumstances, wholly void.⁵ But such an

¹ Dublin, &c., Ry. Co. v. Black, 7 Railway & Canal Cas., 434 (1852); s. c. 8 Exch. 181. Infancy is a personal defense. It is a shield and not a sword. Beardsley v. Hotchkiss, 96 N. Y. 201 (1884). Where an infant allows his name to remain on the register after he becomes of age, he thereby ratifies his subscription. Cork, &c., Ry. Co. v. Cazenove, 10 Q. B. 935 (1847). Cf. Mitchell's Case, L. R., 9 Eq. 363 (1870). A court will not presume that an infant subscriber has avoided his contract, and hence a defense of infancy, in an action on a subscription, without an allegation of avoidance, is ineffectual, and the plaintiff may have judgment. Leeds, &c., Ry. Co. v. Fearnley, 4 Exch. 26 (1849); Curtis' Case, L. R., 6 Eq. 455 (1868). But it has been held, that repudiation before coming of age avoids the contract of subscription *ab initio*, and hence a plea of infancy and of repudiation while an infant, and of notice to the company, that the stock was at their disposal, is a good defense to an action on a subscription. Newry, &c., Ry. Co. v. Coombe, 3 Exch. 565 (1849); s. c. 18 L. J. (Exch.), 325 (1849).

² Musgrave v. Morrison, 54 Md. 161

(1880); Burr v. Wilcox, 22 N. Y. 521 (1860); Granger, &c., Co. v. Vinson, 6 Oregon, 172 (1876); State v. Lehre, 7 Rich. Law, 234 (1854); Hawley v. Upton, 102 U. S. 314 (1880); Davidson v. Grange, 4 Grant's Ch. (N. C.) 377 (1854). Cf. Drover v. Evans, 59 Ind. 454.

³ As where one authorized an agent to subscribe for him for a certain number of shares, and the agent, instead of subscribing, merely entered the name of his principal in the stock book as a stockholder. Here it was held that there having been no actual subscription, there was no liability on the part of the person authorizing the subscription. Granger, &c., Co. v. Vinson, 6 Oregon, 172 (1876). Also, New Brunswick, &c. Co. v. Mugeridge, 4 Hurl. & N. 160 (1859).

In New York it is a penal offense for a person to subscribe for another who does not intend to pay, or to subscribe in the name of a fictitious person. N. Y. Penal Code, § 590.

⁴ Stover v. Flack, 30 N. Y. 64 (1864); Orr v. Bigelow, 14 N. Y. 556 (1856); Colt v. Clapp, 127 Mass. 476 (1879).

⁵ Ticonic, &c., Co. v. Lang, 63 Me. 480 (1874); Pim's Case, 3 De G. & Sm.

unauthorized subscription may be adopted and ratified by the person in whose name it was made without warrant of authority, in such a way as to make it valid and binding.¹ A person subscribing for shares, as agent for another, and in that other's name, but without authority, thereby becomes himself a subscriber in place of the person whose name he signs, or his unauthorized subscription may subject him to an action of damages.²

11 (1849); *Henessey's Case*, 3 Id. 191 (1850); *Ex parte Hall*, 1 McN. & G. 307 (1849). *Cf.* *Chapman & Barker's Case*, L. R., 3 Eq. 361 (1867). And this is equally the rule when it is sought to charge one by such a subscription not in his individual capacity, but only in the capacity of trustee for another. *Ex parte Hall*, *supra*.

¹ *Musgrave v. Morrison*, 54 Md. 161 (1880); *Diman v. Providence, &c., R. R. Co.*, 5 R. I. 130 (1858); *Mississippi, &c., R. R. Co. v. Harris*, 36 Miss. 17 (1858); *Jones v. Milton, &c., Co.*, 7 Ind. 547 (1856); *Philadelphia, &c., R. R. Co. v. Cowell*, 28 Penn. St. 329 (1857); *McCully v. Pittsburgh, &c., R. R. Co.*, 32 Id. 25 (1858). *Cf.* *Putnam v. City of New Albany*, 4 Biss. 365 (1869); *Rutland, &c., R. R. Co. v. Lincoln*, 29 Vt. 206 (1857); *Haslett v. Wotherspoon*, 1 Strobh. (Eq.), 209 (1847). What acts or omissions, short of express ratification, will, in law, suffice to bind one upon such a subscription, is, in general, a question for the jury. *Philadelphia, &c., R. R. Co. v. Cowell*, 28 Penn. St. 329 (1857). *Cf.* *Fox v. Clifton*, 6 Bing. 776 (1830). It is held that silence or failure to object to the subscription for a considerable time after knowledge of it is brought to the subscriber, is evidence of a ratification. *Philadelphia, &c., R. R. Co. v. Cowell*, *supra*; *McHose v. Wheeler*, 45 Penn. St. 32 (1863); *Diman v. Providence, &c., R. R. Co.*, 5 R. I. 130 (1858); *Thompson v. Reno Savings Bank*, 10 Am. & Eng. Corp. Cases, 203 (Nev. 1885); *Sanger v. Upton*, 91 U. S. 56 (1875). But see *Hume v. Commercial Bank*, 9 Lea, 728 (1882). And to authorize a proxy to vote, the stock may be sufficient to ratify such a subscription. *McCully v. Pittsburgh, &c., R. R. Co.*, 32 Penn. St. 25 (1858). *Contra*, *McClelland v. Whiteley*, 11 Biss. 444 (1883). But a mere declaration to strangers, by the person in whose name

the subscription had been made, that he had taken that amount of stock, is not a ratification of the subscription. *Rutland, &c., R. R. Co. v. Lincoln*, 29 Vt. 206 (1857). And even the fact that one whose name had been in this way put down as a subscriber, was a director in the corporation, was held not, *in se*, to imply knowledge that his name was on the books as a subscriber. *In re Wincham, &c., Co.*, L. R., 9 Chan. Div. 329 (1878). *Cf.* *Fox v. Clifton*, 6 Bing. 776 (1830). But as a rule, it is believed, that accepting the office of a director would, in this country, be held a sufficient ratification of such a subscription, in the absence of any other. This is expressly declared to be the rule in Tennessee and elsewhere. *Moses v. Ocoee Bank*, 1 Lea, 398 (1878); *Danbury, &c., R. R. Co. v. Wilson*, 22 Conn. 435 (1853); *cf.* *Fry v. Lexington, &c., R. R. Co.*, 2 Metc. (Ky.), 314 (1859). *Contra*, *Hume v. Commercial Bank*, 9 Lea, 728 (1882). For a full consideration of estoppel in respect to shares ownership, see the note to case of *Griswold v. Seligman*, 4 Am. and Eng. R. R. Cases, 371, 384 (1880).

² *Salem, &c., Corp. v. Ropes*, 9 Pick. 187 (1829). In some jurisdictions it is held that by such a subscription the subscriber makes himself personally liable as a subscriber. *Union Hotel Co. v. Hersee*, 79 N. Y. 454 (1880); *State v. Smith*, 48 Vt. 266. See also *Burr v. Wilcox*, 22 N. Y. 551 (1860); *Troy, &c., R. R. Co. v. Warren*, 18 Barb. 310 (1854); *Cox's Case*, 4 De G., J. & S. 53 (1863); distinguishing *King's Case*, L. R. 6 Chan. 196 (1871). And a person subscribing as a promoter for shares in the name of a fictitious or irresponsible person makes himself liable absolutely on such subscription. *Cox's Case*, *supra*; *Pugh & Sharman's Case*, L. R., 13 Eq. 566 (1872). So also if the stock be assigned to a fictitious or irresponsible person after subscription, the sub-

§ 66. *Subscriptions taken by an unauthorized agent of the corporation.*—A subscription taken by a person who has no authority from the corporation to take subscriptions is not in general enforceable.¹ But such a subscription may, by acceptance and ratification on the part of the corporation, be validated, and the subscriber made liable as though the subscription had been regularly taken.²

§ 67. *Agreements to subscribe made before organization.*—A distinction has been attempted in some courts between a subscription for stock in a company already organized and an agreement to subscribe for stock in a company to be subsequently organized and incorporated. Where, previously to the organization of the company, parties who expect to subscribe for stock sign an agreement between themselves alone, to take stock in the company when organized, this has been held to be a contract which the corporation itself, after coming into being, cannot specifically enforce.³ This is upon the theory that the contract was not made with the corporation, which indeed was not in existence when the paper was signed, and that the corporation, being a stranger to it, cannot enforce it.⁴ It is sometimes

scriber will not thereby be released. *Muskingum, &c., Co. v. Ward*, 13 Ohio, 120 (1844).

¹ *Essex, &c., Co. v. Collins*, 8 Mass. 292 (1811); *Shurtz v. Schoolcraft, &c., R. R. Co.*, 9 Mich. 269 (1861); *Carlisle v. Saginaw, &c., R. R. Co.*, 27 Id. 315 (1873); *Troy, &c., R. R. Co. v. Warren*, 18 Barb. 310 (1854); *cf. Grangers', &c., Co. v. Vinson*, 6 Oregon, 174 (1876); *Howard's Case*, L. R. 1 Chan. 561 (1866). *Contra*, *Northeastern R. R. Co. v. Rodrigues*, 10 Rich. Law, 278 (1857).

² *Walker v. Mobile, &c., R. R. Co.*, 34 Miss. 245 (1857); *Mobile, &c., R. R. Co. v. Yandal*, 5 Sneed, 294 (1858); *Judah v. American, &c., Co.*, 4 Ind. 333.

³ *Lake Ontario, &c., R. R. Co. v. Curtiss*, 80 N. Y. 219 (1880); *Strasburg R. R. Co. v. Echternacht*, 21 Penn. St. 220 (1853); *Mt. Sterling, &c., Co. v. Little*, 14 Bush, 429 (1879); *California, &c., Co. v. Schafer*, 57 Cal. 396 (1881); *Poughkeepsie, &c., Co. v. Griffin*, 24 N. Y. 150 (1860); *Charlotte, &c., R. R. Co. v. Blakeley*, 3 Strobb. Law, 245 (1848); *Pittsburgh, &c., R. R. Co. v. Gazzam*, 32 Penn.

St. 340 (1858); *Wallingford, &c., Co. v. Fox*, 12 Vt. 304 (1840); *Chase v. Sycamore, &c., R. R. Co.*, 38 Ill. 215 (1865). *Cf. Sewall v. Eastern R. R. Co.*, 9 Cush. 5 (1851); *Stowe v. Flagg*, 72 Ill. 397 (1874); *Goff v. Winchester College*, 6 Bush, 443 (1869); *Perkins v. Union Button Hole, &c., Co.*, 12 Allen, 273 (1866); *Carlisle v. Saginaw, &c., R. R. Co.*, 27 Mich. 315 (1873); *Dayton, &c., Co. v. Coy*, 13 Ohio St. 84 (1861).

⁴ Speaking to this point, and declaring the rule in Canada, O'Connor, J., said: "The defendant cannot, I think, be held to have subscribed stock in the capital of a company which at the time was not in existence. Nor can it be said that he made a contract with the company which bound him to take stock *in futuro*. There is no statute in this country that I know of, nor has one been referred to by counsel, like the English act, which makes such a stock list available to the company when incorporated. But here the company and the stock were only *in prospectu*, and not *in esse*; and how can this company, then

held that while the action in equity to compel the subscriber to take up and pay for stock in the corporation will not lie, an action at law for damages may be brought by the corporation against any one who, having signed the preliminary agreement, fails or refuses to take and pay for the stock.¹ And that the measure of damages for such a breach of contract to subscribe for stock is the difference between the par and market value of the stock involved.² But it is clearly the better rule that an agreement by one person with others, before incorporation, to subscribe and pay for stock in the proposed company, is a valid contract of subscription, and is enforceable by the corporation itself after it comes

only *in posse*, be a party to, and stock not *in esse* be the subject of, a contract *in presenti*?" Citing *Kelner v. Baxter*, L. R. 2 C. P. 174 (1866); *Melhado v. The Porto Alegre, &c., Ry. Co.*, L. R. 9 C. P. 503 (1874). So also it is held that incorporation is a necessary condition precedent to an enforcement of such antecedent subscription. *Dorris v. Sweeney*, 60 N. Y. 463 (1875); *Richmond Street Ry. Co. v. Reed*, 83 Ind. 9 (1882); *Stoops v. Greenburgh, &c., Co.*, 10 Ind. 47 (1857); *Low v. Connecticut, &c., R. R. Co.*, 45 N. H. 370 (1864); *Monterey, &c., R. R. Co. v. Hildreth*, 53 Cal. 123 (1878). *Cf.* *Marlborough, &c., R. R. Co. v. Arnold*, 9 Gray, 159 (1857); *Diman v. Providence, &c., R. R. Co.*, 5 R. I. 130 (1858); *Danbury, &c., R. R. Co. v. Wilson*, 22 Conn. 435 (1853); *Buffalo, &c., R. R. Co. v. Hatch*, 20 N. Y. 157 (1859); *Garrett v. Dillsburg, &c., R. R. Co.*, 78 Penn. St. 465 (1875); *Midland, &c., Ry. Co. v. Gordon*, 16 Me. & W. 804 (1847). *Contra*, *Oregon, &c., R. R. Co. v. Scroggin*, 3 Oregon, 161 (1867). See on this subject Chapter X.

¹ *Quick v. Lemon*, 105 Ill. 578 (1883); *Thrasher v. Pike Co., &c., R. R. Co.*, 25 Id. 393 (1861); *Rhey v. Ebensburg, &c., R. R. Co.*, 27 Penn. St. 261 (1856); *cf.* *Mt. Sterling, &c., R. R. Co. v. Little*, 14 Bush, 429 (1879); *People v. Holden*, 82 Ill. 93 (1876); *Ottawa, &c., R. R. Co. v. Black*, 79 Id. 262 (1875).

² *Thrasher v. Pike Co., &c., R. R. Co.*, 25 Ill. 393 (1861). It seems also that such an action of damages might be brought by one of the signers of the preliminary agreement, against any other signer who refused to take and pay for stock after the incorporation of the com-

pany, and that the measure of damages in this case would be, not the amount subscribed but the damage sustained by the person suing. *Lake Ontario, &c., R. R. Co. v. Curtiss*, 80 N. Y. 219 (1880). In Pennsylvania, a statute which authorized a corporation to enforce such an agreement specifically has been held unconstitutional. *Pittsburgh, &c., R. R. Co. v. Gazzam*, 32 Penn. St. 340 (1858). It is elsewhere said that a subscription preliminary to organization is no contract, but merely a means of bringing the parties together. *Poughkeepsie, &c., R. R. Co. v. Griffin*, 24 N. Y. 150 (1860). *Cf.* *New Brunswick, &c., Co. v. Muggeridge*, 4 Hurl. & N. 160 (1859). Or a mere continuing offer to subscribe upon the organization of the company, and that it must be accepted by the corporation before suit can be brought to enforce it. *Starrett v. Rockland, &c., R. R. Co.*, 65 Me. 374 (1876). In Indiana such a subscription inures to the benefit of the corporation upon the filing of the articles of association. *Miller v. Wild Cat, &c., Co.*, 52 Ind. 51 (1875). *Cf.* *Drover v. Evans*, 59 Id. 454. And in New York it is said that the right to membership in the proposed corporation is a sufficient consideration for the subscriber's liability upon a subscription for stock made before the incorporation of the company, and that immediately upon incorporation the company acquires a vested interest in the agreement to subscribe. *Lake Ontario, &c., R. R. Co. v. Mason*, 16 N. Y. 451, 463 (1857). But an agreement to place shares will not be construed as an engagement to take shares. *Gorrissen's Case*, L. R. 8 Chan. 507 (1873).

into being.¹ The signing of the subscription paper is an implied promise to pay for the shares.²

§ 68. *In New England an express promise necessary.*—

There is a line of cases, especially in New England, which hold that a suit will lie to enforce a subscription only when the act of incorporation or the general law authorizes it, or when an express promise to pay has been distinctly made.³ The reason of this

¹ Reformed, &c., *Church v. Brown*, 17 How. Pr. 287 (1859); *Penobscot, &c., R. R. Co. v. Dummer*, 40 Me. 172 (1856); *Athol, &c., Co. v. Carey*, 116 Mass. 471 (1875); *Ashuelot, &c., Co. v. Hoit*, 56 N. H. 548 (1876); *Cross v. Pinckneyville, &c., Co.*, 17 Ill. 54 (1855); *Griswold v. Trustees, &c.*, 26 Id. 41 (1861); *Stone v. Great Western, &c., Co.*, 41 Id. 85 (1866); *Proprietors, &c. v. Dickinson*, 6 Gray, 586 (1856); *Heaston v. Cincinnati, &c., R. R. Co.*, 16 Ind. 275 (1861); *Eastern, &c., Co. v. Vaughan*, 14 N. Y. 546 (1856); *Buffalo, &c., R. R. Co. v. Gifford*, 87 Id. 294 (1882); *Id. v. Clark*, 22 Hun, 359 (1880); *Peninsular, &c., R. R. Co. v. Duncan*, 28 Mich. 130 (1873); *Buffalo, &c., R. R. Co. v. Dudley*, 14 N. Y. 336 (1856); *Dayton v. Borst*, 31 Id. 435 (1865); *Rensselaer, &c., R. R. Co. v. Barton*, 16 Id. 457 (1857); *Lake Ontario, &c., R. R. Co. v. Mason*, 16 Id. 451 (1857); *Essex, &c., Co. v. Tuttle*, 2 Vt. 393 (1830); *Kirksey v. Florida, &c., R. R. Co.*, 7 Fla. 23 (1857); *Beene v. Cahawba, &c., R. R. Co.*, 3 Ala. 660 (1842); *Selma, &c., R. R. Co. v. Tipton*, 5 Id. 787 (1843); *Hartford, &c., R. R. Co. v. Kennedy*, 12 Conn. 499 (1838); *Thigpen v. Mississippi, &c., R. R. Co.*, 32 Miss. 347 (1856); *Gill v. Kentucky, &c., Co.*, 7 Bush, 635 (1870); *Cucullu v. Union Ins. Co.*, 2 Rob. (La.) 573 (1842); *Union, &c., Co. v. Jenkins*, 1 Caines, 381 (1803); *Goshen, &c., Co. v. Hurtin*, 9 Johns. 217 (1812); *Dutchess, &c., Co. v. Davis*, 14 Id. 238 (1817); *Spear v. Crawford*, 14 Wend. 20 (1835); *Harlem, &c., Co. v. Seixas*, 2 Hall (N. Y. Super. Ct.), 504 (1829); *Nulton v. Clayton*, 54 Iowa, 425 (1880); *Worcester, &c., Co. v. Willard*, 5 Mass. 80 (1809); *Stanton v. Wilson*, 2 Hill, 153 (1841); *Sagory v. Dubois*, 3 Sandf. Chan. 466 (1846); *Palmer v. Lawrence*, 3 Sandf. Super. Ct. 161 (1849); *Twin Creek, &c., Co. v. Lancaster*, 79 Ky. 552 (1881); *cf. Thompson v. Page*, 1 Metc. 565 (1840); *Ives v. Sterling*, 6 Id. 310 (1843); *Robinson v. Edinboro' Academy*, 3 Grant's Cas. 107 (1861); *Ed-*

inboro' Academy v. Robinson, 37 Penn. St. 210 (1860); *Hutchins v. Smith*, 46 Barb. 235 (1865); *Valk v. Crandall*, 1 Sandf. Chan. 179; *People, &c., Co. v. Balch*, 8 Gray, 303; *Chater v. San Francisco, &c., Co.*, 19 Cal. 219 (1861); *Highland, &c., Co. v. McKean*, 11 Johns. 98 (1814); *Tar River, &c., Co. v. Neal*, 3 Hawks (N. C.), 520 (1825); *Klein v. Alton, &c., R. R. Co.*, 13 Ill. 514 (1851); *Banet v. Id.*, 13 Id. 504 (1851); *Sanger v. Upton*, 91 U. S. 56 (1875); *Kidwelly, &c., Co. v. Raby*, 2 Price (Eng.), 93 (1816). See also *Weiss v. Mauch Chunk, &c., Co.*, 58 Penn. St. 295 (1868).

² *Dexter, &c., Co. v. Millerd*, 3 Mich. 91 (1854); *Upton v. Tribilcock*, 91 U. S. 45 (1875); *Webster v. Upton*, 91 Id. 65 (1875). For an elaborate discussion of the distinction between an express and an implied promise to pay for shares subscribed, and the legal consequences of such promises, see *Northern R. R. Co. v. Miller*, 10 Barb. 260, 268 (1851). *Willard, J.* In the briefs and the opinion in this case many authorities are carefully collected. And even when the act of incorporation or the general law provides for forfeiture of the shares upon non-payment, the corporation may waive the right to forfeit, and proceed personally upon the contract of subscription, inasmuch as the remedy by forfeiture is now conceded to be merely cumulative. See the Chapter on Forfeiture, *infra*. The liability of the subscribers to pay in the amount of capital subscribed by them, is several and not joint, and hence a joint action to enforce will not lie. *Price v. Grand Rapids, &c., R. R. Co.*, 18 Ind. 137 (1862); *Herron v. Vance*, 17 Id. 595 (1861); *Thompson v. Reno Savings Bank*, 10 Am. & Eng. Corp. Cases, 203 (Nev. 1885).

³ *Kennebec, &c. R. R. Co. v. Kendall*, 31 Me. 470 (1850); *Belfast, &c. R. R. Co. v. Cottrell*, 66 Id. 185 (1876); *Katowa Land Co. v. Holley*, 129 Mass. 540 (1880); *Mechanics, &c. Co. v. Hall*, 121 Id. 272

rule seems to have been the hardship that otherwise might be imposed upon the subscriber, because in the earliest charters a share of stock was not limited specifically in amount, even though the whole capital stock was to be divided into a certain fixed number of shares. In consequence, when the full prescribed number of shares were not subscribed, those who did subscribe became liable until the full capital stock had been paid in. This rule is first found in a line of decisions which were made in cases growing out of the formation of early turnpike or highway bridge corporations.¹ Consequently it was held to be no more than just to allow subscribers, if the assessments become grievous, or they weary of the enterprise, to withdraw from the company upon forfeiting their stock, and that any other rule is, in some instances, almost the enforcement of a penalty.²

(1876). *Cf. Seymour v. Sturgess*, 26 N. Y. 134 (1862); *Fort Edward, &c. Co. v. Payne*, 17 Barb. 567 (1854); *Andover, &c. Co. v. Gould*, 6 Mass. 40 (1809); *Essex, &c. Co. v. Collins*, 8 Id. 292 (1811). In some of the States, accordingly, we find that it has, from an early day, been held that unless the subscriber, by an express promise in his subscription, agreed to pay the amount of his subscription, or unless the act of incorporation itself declared that the subscriber should be bound to pay, no action could be maintained by the corporation to enforce the subscription. In Pennsylvania, a statute which authorized a corporation to enforce such a subscription was held unconstitutional. *Pittsburgh, &c. R. R. Co. v. Gazzam*, 32 Penn. St. 340 (1858).

¹ *Worcester, &c. Turnpike Co. v. Willard*, 5 Mass. 80 (1809); *Andover, &c. Turnpike Co. v. Gould*, 6 Mass. 40 (1809); *New Bedford, &c. Turnpike Co. v. Adams*, 8 Id. 138 (1811); *Essex, &c. Co. v. Collins*, 8 Id. 292 (1811); *Franklin, &c. Co. v. White*, 14 Id. 286 (1817). See also the same rule applied to cases of subscription to the capital stock of railway and other corporations. *Kennebec, &c. R. R. Co. v. Kendall*, 31 Me. 470 (1850); *Belfast, &c. R. R. Co. v. Moore*, 60 Id. 561 (1871); *New Hampshire, &c. R. R. Co. v. Johnson*, 30 N. H. 390 (1855); *White, &c. R. R. Co. v. Eastman*, 34 Id. 124 (1856); *Essex, &c. Co. v. Tuttle*, 2 Vt. 393 (1830); *Connecticut, &c. R. R. Co. v. Bailey*, 24 Id. 465. *Cf. Tilsenburgh, &c. Co. v. Goodrich*, 8 Ontario (Q. B. Div.), 565 (1885).

² *Andover, &c. Co. v. Gould*, 6 Mass. 40 (1809); *Mechanics, &c. Co. v. Hall*, 121 Id. 272 (1876).

In those jurisdictions where the right of the corporation to enforce these subscriptions specifically is maintained, it is held that no formal acceptance of the subscription by the corporation is necessary to the maintenance of the suit. *Buffalo, &c. R. R. Co. v. Dudley*, 14 N. Y. 336 (1856); *Lake Ontario, &c. R. R. Co. v. Mason*, 16 Id. 451 (1857); *Buffalo, &c. R. R. Co. v. Clark*, 22 Hun. 359 (1880); *Northern R. R. Co. v. Miller*, 10 Barb. 260 (1851); *Spear v. Crawford*, 14 Wend. 20 (1835); *Hughes v. Antietam, &c. Co.*, 34 Md. 316 (1870). *Cf. Penobscot, &c. R. R. Co. v. Dummer*, 40 Me. 172 (1855). *Contra, Gleaves v. Brick Church, &c. Co.*, 1 Sneed. 491 (1853); *Starrett v. Rockland, &c. R. R. Co.*, 65 Me. 374 (1876). "A subscription to take shares in the stock of a corporation to be formed, enures to the benefit of that corporation when formed." *Griswold v. The Trustees, &c.*, 26 Ill. 41 (1861); *Cross v. Pinckneyville, &c. Co.*, 17 Id. 54 (1855); *Miller v. Wild Cat, &c. Co.*, 52 Ind. 51 (1875). It is accordingly said that a contract to pay in installments a certain sum as work on a railroad progressed, stock therefor to be delivered by the corporation to the payor upon full payment of the amount promised, while it is not technically a subscription for stock, is a valid and enforceable undertaking, and that stock must be tendered before a suit can be maintained. *Clark v. Continental, &c. Co.*, 57 Ind. 134 (1877). So also a subscription made before or

§ 69. *A subscription for shares implies a promise to pay for them.*—It is a general rule in most of the States, and in the Supreme Court of the United States, that a subscription for shares of stock does not require an express promise, but implies a promise on the part of the subscriber to pay for them.¹ But in Massachusetts, Vermont, and Maine, this rule does not obtain, and it is held in those jurisdictions that a subscription for shares subjects the subscriber only to the penalties imposed by the statute under which the corporation is organized, that the undertaking to take up the shares is one thing, and the undertaking to pay for them another, and that, where there is no express promise to pay for the shares in the subscription, no action can be maintained.²

§ 70. *Considerations for such agreements.*—It has been found a matter of considerable practical difficulty to determine precisely and satisfactorily upon what consideration an agreement to take stock in a company to be subsequently organized and incorporated, can be founded and enforced. Different courts

organization becomes binding by action on the part of the subscriber as a stockholder after organization. *Buffalo, &c. R. R. Co. v. Gifford*, 87 N. Y. 294 (1882).

But an offer or agreement to subscribe is revoked by death where it has not yet been accepted by the corporation. *Wallace v. Townsend*, 43 Ohio St. 537 (1885); *Sedalia, W. & S. Ry. Co. v. Wilkinson*, 83 Mo. 235 (1884).

¹ *Upton v. Tribilcock*, 91 U. S. 45 (1875); *Hawley v. Upton*, 102 U. S. 314 (1880); *Webster v. Upton*, 91 Id. 65 (1875); *Beene v. Cahawba, &c., R. R. Co.*, 3 Ala. 660 (1842); *Fry v. Lexington, &c., R. R. Co.*, 2 Metc. (Ky.), 314 (1859); *Gill v. Kentucky, &c., Co.*, 7 Bush, 635 (1870); *Mt. Sterling, &c., Co. v. Little*, 14 Id. 429 (1879); *Chase v. Railroad Co.*, 5 Lea (Tenn.), 415 (1880); *Small v. Herkimer, &c., Co.*, 2 N. Y. 330 (1849); *Lake Ontario, &c., R. R. Co. v. Mason*, 16 Id. 451 (1857); *Dayton v. Borst*, 31 Id. 435 (1865); *Waukon, &c., R. R. Co. v. Dwyer*, 49 Iowa, 121 (1878); *Nulton v. Clayton*, 54 Id. 425 (1880); *Miller v. Wild Cat, &c., Co.*, 52 Ind. 51 (1875); *Mitchell v. Beckman*, 64 Cal. 117 (1883); *Merrimac, &c., Co. v. Levy*, 54 Penn. St. 227 (1867). Even though the corporation have the power to forfeit the shares for non-payment. *Hughes v. Antietam,*

&c., Co., 34 Md. 316 (1870); *Dexter, &c., Co. v. Millerd*, 3 Mich. 91 (1854).

² *Andover, &c., Co. v. Gould*, 6 Mass. 40 (1809); *Atlantic, &c., Mills v. Abbott*, 9 Cush. 423 (1852); *Mechanics, &c., Co. v. Hall*, 121 Mass. 272 (1876); *Katama, &c., Co. v. Jernegon*, 126 Id. 156 (1879); *Boston, &c., R. R. Co. v. Wellington*, 113 Id. 79 (1873); *Connecticut, &c., R. R. Co. v. Bailey*, 24 Vt. 465; *Belfast, &c. R. R. Co. v. Moore*, 60 Me. 56 (1872); *Belfast, &c., R. R. Co. v. Cottrell*, 66 Id. 185 (1876); *Kennebec &c., R. R. Co. v. Kendall*, 31 Id. 470 (1850); *Buckfield, &c., R. R. Co. v. Irish*, 39 Id. 44 (1854). *Cf. Townsend v. Goewey*, 19 Wend. 424 (1838); s. c. 32 Am. Dec. 514. See also *Essex, &c., Co. v. Collins*, 8 Mass 292 (1871); *New Hampshire, &c., R. R. Co. v. Johnson*, 30 N. H. 390 (1855); *Russell v. Bristol*, 49 Conn. 251 (1881); *Odd Fellows, &c., Co. v. Glazier*, 5 Harr. (Del.), 172 (1848); *Stokes v. Lebanon, &c., Co.*, 6 Humph. 241 (1845); *City Hotel v. Dickinson*, 6 Gray, 586 (1866); *Seymour v. Sturgess*, 26 N. Y. 134 (1862). In Maine an agreement to "take and fill" a number of shares, has been held equivalent to an express promise to pay for them. *Buckfield, &c., R. R. Co. v. Irish*, 39 Me. 44 (1854); *Penobscot, &c., R. R. Co. v. Bartlett*, 12 Gray, 244 (1858).

have reached different conclusions, and the question is not yet settled. Accordingly we find it held that the right to membership in the proposed corporation, and the probable advantages to be derived from membership in such a company, are a sufficient consideration to make the subscriber liable.¹ So also it is held that the stock to be received, and the probable dividends thereon, are a sufficient consideration to support the promise.² But without reference to the question of consideration, and in the absence of all considerations, it is said that an obligation to pay for shares subscribed, is conclusively implied from the fact of subscription.³ "The consideration to sustain such a promise is raised by inference of law from the subscription itself, and the privileges

¹ *Lake Ontario, &c., R. R. Co. v. Mason*, 16 N. Y. 451 (1857); *Fort Edward, &c., Co. v. Payne*, 17 Barb. 567 (1854); *Hamilton, &c., Co. v. Rice*, 7 Id. 157 (1849); *Schenectady, &c., R. R. Co. v. Thatcher*, 11 N. Y. 102, 108 (1854); *Barnes v. Perine*, 12 Id. 18 (1854); *Osborn v. Crosby*, 63 N. H. 583 (1885). See also *Stewart v. Trustees of Hamilton College*, 2 Denio, 403 (1845); *Hamilton College v. Stewart*, 1 N. Y. 581 (1848). "It is well settled," said Hand, J., in the case of *Fort Edward, &c., Co. v. Payne*, 17 Barb. 567 (1854), "that a subscription to the capital stock of any company, from the membership of which a shareholder may derive pecuniary advantage, gives to the subscriber such an interest, or will support a promise to pay for the shares. Such an enterprise is a combination of means for mutual profit, and is in no sense a gift or promise without consideration." And elsewhere it is said, that "the advantages to be derived from being a member of such a company, and of the consequent right to participate in the pecuniary dividends, is a positive benefit, and where the agreement secures that advantage to the subscriber, on the organization of the company, the objection of a want of consideration cannot be made with success." *Hamilton, &c., Co. v. Rice*, 7 Barb. 157 (1849), adopted by *Brown, J.*, in *Lake Ontario, &c., R. R. Co. v. Mason*, 16 N. Y. 451, 463 (1857).

² *Schenectady, &c., R. R. Co. v. Thatcher*, 11 N. Y. 102, 108 (1854); *Bish v. Bradford*, 17 Ind. 490 (1861); *New Albany, &c., R. R. Co. v. Fields*, 10 Id. 187 (1858); *Fry v. Lexington, &c., R. R. Co.*, 2 Metc. (Ky.), 314 (1859). That the interest acquired by subscrib-

ing for shares of the capital stock is a good consideration for the promise to pay for them, *Union, &c., Co. v. Jenkins*, 1 Caines, 381 (1803); *Selma, &c., R. R. Co. v. Tipton*, 5 Ala. 787 (1843) (a full and learned opinion). *Cf. Goshen, &c., Co. v. Hurin*, 9 Johns. 217 (1812); *Danbury, &c., R. R. Co. v. Wilson*, 22 Conn. 435, (1853); *East Tennessee, &c., R. R. Co. v. Gammon*, 5 Sneed, 567. And again that the prior proceedings and acts of the parties are a legal basis for the promise to pay; also that the partial execution of the purpose designed by the charter is a sufficient consideration. *Kennebec, &c., R. R. Co. v. Palmer*, 34 Me. 366 (1852); *McAuley v. Billenger*, 20 Johns. 89 (1822); *Amherst Academy v. Cowls*, 23 Mass. 427 (1828); *Ohio, &c., College v. Higgins*, 16 Ohio St. 20 (1864). *Cf. McCally v. Pittsburgh, &c., R. R. Co.*, 32 Penn. St. 25 (1858). In Minnesota, the implied promise to issue the stock is declared to be the consideration for the promise to pay for it. *St. Paul, &c., R. R. Co. v. Robbins*, 23 Minn. 439 (1877). And in Kentucky, it is held that the promise by each of the subscribers is a sufficient consideration for the promises of the others. *Twin Creek, &c., Co. v. Lancaster*, 79 Ky. 552.

³ *East Tennessee, &c., R. R. Co. v. Gammon*, 5 Sneed, 567; *Barker v. Bucklin*, 2 Denio, 45 (1846); *Spear v. Crawford*, 14 Wend. 20 (1835); *Cole v. Ryan*, 52 Barb. 68 (1868); *Amherst Academy v. Cowls*, 23 Mass. 427 (1828); *Thompson v. Page*, 42 Id. 565 (1840); *Upton v. Tribilcock*, 91 U. S. 45 (1875). *Cf. Northern, &c., R. R. Co. v. Miller*, 10 Barb. 260 (1851); *Dutchess, &c., R. Co. v. Davis*, 14 Johns. 238 (1817).

thereby conferred; and from the same circumstance the law will infer a duty to pay for the stock, and an implied obligation of equal force with an express contract."¹

The consideration does not depend upon the motive which induced the subscription. The consideration for the subscription, in point of law, is one thing, and the motive, or those considerations of interest or policy that induced the subscription, quite another thing.²

§ 71. *Subscriptions delivered in escrow.*—Subscriptions for shares may be made and delivered in escrow to an agent of the corporation who is engaged in taking subscriptions,³ or to a director of the corporation.⁴ But a delivery in escrow to a commissioner is bad, and a subscription so delivered is absolute.⁵ Delivery of a subscription in escrow to become absolute on performance of certain conditions by the corporation, differs from a conditional subscription in this, that a subscription in escrow is, strictly speaking, no subscription. As in the case of a deed delivered in

¹ *East Tennessee, &c., R. R. Co. v. Gammon, supra*. So also it is held that there is an implied promise on the part of a transferee of shares to pay calls upon such stock while he continues the owner, and that such implied promise to pay is of equal rank, and involves the same duty as the original promise of the original subscriber for the shares. *Webster v. Upton*, 91 U. S. 65 (1875); *Palmer v. Lawrence*, 3 Sandf. Super. Ct. 161 (1849); *Bend v. Susquehanna, &c., Co.*, 6 Harris & J. 128 (1823); *Hall v. United States Ins. Co.*, 5 Gill. 484 (1847); *Hartford, &c., R. R. Co. v. Boorman*, 12 Conn. 530 (1838); *Huddersfield Canal Co. v. Buckley*, 7 Term Rep. 36 (1796). *Cf. Delaware, &c., Co. v. Sansom*, 1 Binn. 70 (1803); *Palmer v. Ridge, &c., Co.*, 34 Penn. St. 288 (1859); *Seymour v. Sturges*, 26 N. Y. 134 (1862). Speaking of the legal significance of a transfer of shares. *Duer, J.*, said: "The transaction, in the technical language of the civil law, was a *novation*, the substitution of one debtor for another, and in all such cases the original debt is just as valid a consideration for the new promise or security as for that for which it is substituted." *Palmer v. Lawrence*, 3 Sandf. Super. Ct. 161, 164 (1849). The liability of a transferee of stock is treated of fully in Ch. XV.

² So, where a defendant urged that, inasmuch as the road to the stock of which

he had subscribed, and upon which he was sued, had not been located where he was assured it would be when he made his subscription, that the consideration for his subscription had failed, it was held that this was a confusion of ideas, and that such an argument confounded motive with consideration. The court said: "The motive of the defendant in subscribing may have been to secure a road where he supposed this was to be located. The consideration of his subscription was the stock to which the payment would entitle him. There has been no failure of consideration." *Miller v. Wild Cat, &c., Co.*, 52 Ind. 51, 64 (1875). See also *Andover, &c., Co. v. Gould*, 6 Mass. 39, 44 (1809); *Parker v. Northern, &c., R. R. Co.*, 33 Mich. 23 (1875); *Ill. River R. R. Co. v. Zimmer*, 20 Ill. 654 (1858).

³ *Cass v. Pittsburgh, &c., R. R. Co.*, 80 Penn. St. 31.

⁴ *Ottawa, &c., R. R. Co. v. Hall*, 1 Bradw. (Ill.) 612 (1878).

⁵ *Wight v. Shelby R. R. Co.*, 16 B. Mon. 4 (1855). It is the rule in Kentucky that to become effectual as an escrow the delivery must be to a third person. *Wight v. Shelby R. R. Co., supra*. But in Pennsylvania it seems the rule is otherwise. *Cass v. Pittsburgh, &c., R. R. Co., supra*. And so in Illinois. *Ottawa, &c., R. R. Co. v. Hall, supra. Cf. Price v. Pittsburgh, &c., R. R. Co.*, 34 Ill. 36.

escrow, no estate passes until the second delivery. So, in the case of a subscription delivered in escrow, there is no subscription until a second delivery, and the depositary can only deliver it up on performance of the condition.¹ So, also, a subscriber may show by parol an agreement with an agent of the corporation, that his subscription to blank paper should not be a subscription until he had seen and approved the heading of the subscription paper.²

§ 72. *Subscriptions in excess of the capital stock.*—In general, after the full amount of stock provided for in the act of incorporation has been subscribed, any further subscriptions are void.³ When all the capital stock of a corporation is subscribed for and taken at the time the articles of association are filed, and the certificate of incorporation, made and filed as required by law, specifies the names of the stockholders, no subsequent subscribers, by merely writing their names in the corporation book and affixing a number of shares to their respective names, can acquire a right to any shares of stock, or become, by such an act, stockholders of the corporation. The corporation, in such a case, has no stock at its disposal, unless some part of that already subscribed come back to it by forfeiture, and no person can become a stockholder except by purchase from one of the original subscribers, or his assignee, and by a regular assignment of the stock.⁴

It is frequently, however, provided, in the act of incorporation, that, in case of an excess of subscriptions beyond the prescribed amount of capital stock, the commissioners may, in their discretion, so apportion or distribute the stock that each subscriber may have allotted to him a certain proportion of the stock—the number of shares to be determined by the ratio of his subscription to the whole amount subscribed. In such a case sub-

¹ *Ottawa, &c., R. R. Co. v. Hall*, 1 Bradw. (Ill.) 612 (1878); *Ashtabula, &c., R. R. Co. v. Smith*, 15 Ohio St. 328 (1864). It is competent to show by parol that a subscription was delivered in escrow. The Court of Appeals of Illinois declares that a contrary rule is not sustained by any respectable authority. *Ottawa, &c., R. R. Co. v. Hall, supra*. Cf. *Tonica, &c., R. R. Co. v. Stein*, 21 Ill. 96 (1859);

Jewell v. Rock River, &c., Co., 101 Id. 57 (1881).

² *Bucher v. Dillsburg, &c., R. R. Co.*, 76 Penn. St., 306 (1874). Cf. *Brewers, &c., Ins. Co. v. Burger*, 10 Hun, 56 (1877).

³ *Lathrop v. Kneeland*, 46 Barb. 432 (1866); *Mackley's Case*, L. R. 1 Chan. Div. 247 (1875).

⁴ *Lathrop v. Kneeland, supra*.

scriptions in excess of the prescribed capital stock are good *pro tanto*.¹

But after the organization of the corporation the duty to apportion the stock, if there has been an oversubscription, belongs to the corporation and not to the commissioners.² And, in the absence of statutory authority, the commissioners, even before organization, have no general power, if they receive excessive subscriptions, to reduce proportionally all the subscriptions and apportion the stock. It is their only duty to take subscriptions up to the full amount of the prescribed capital and to refuse anything beyond that.³ Neither can the corporation, if it have issued the full amount of the stock, recover on subscriptions in excess, the subscriber acquires no title by such a subscription, and corporate creditors can enforce no liability thereon.⁴

§ 73. *Proof of subscription or stockholdership*.—In order to hold one liable as a subscriber to stock in a stock corporation, it must be shown that he subscribed a contract to take stock in the company, or that he authorized some competent person to subscribe such a contract for him, or that, with knowledge that a subscription had been made in his name, he ratified the act.⁵ It is presumptive evidence that one is a subscriber or a stockholder when his name appears on the books of the company in either of

¹ Buffalo, &c., R. R. Co. v. Dudley, 14 N. Y. 336 (1856); Crocker v. Crane, 21 Wend. 211 (1839). Cf. State v. Lehre, 7 Rich. Law, 234 (1854); Danbury, &c., R. R. Co. v. Wilson, 22 Conn. 435, 454 (1853); Van Dyke v. Stout, 8 N. J. Eq. 333 (1850).

If the commissioners do not properly apportion the stock, an aggrieved subscriber may apply to a court of equity for relief. Walker v. Devereaux, 4 Paige, 229 (1833); Meads v. Walker, Hopk. Ch. 661 (1825); but see Ferguson v. Wilson, L. R. 2 Ch. 77 (1866).

Where an apportionment is provided for in the event of an excess of subscriptions, it is said that the contract of subscription is not complete until the apportionment is made; that there can be neither stockholders nor corporation prior to the apportionment. Walker v. Devereaux, 4 Paige, 229 (1833); Crocker v. Crane, 21 Wend. 211 (1839); Burrows v. Smith, 10 N. Y. 550 (1853). Cf. Buffalo, &c., R. R. Co. v. Dudley, 14 N. Y. 336, 346 (1856).

² State v. Lehre, 7 Rich. Law, 234 (1854).

³ Van Dyke v. Stout, 8 N. J. Eq. 333 (1850). Cf. Crocker v. Crane, 21 Wend. 211 (1839).

⁴ Oler v. Baltimore, &c., R. R. Co., 41 Md. 583 (1874); Burrows v. Smith, 10 N. Y. 550 (1853). Cf. Smith v. Bangs, 15 Ill. 399 (1854). It is held also that corporate officers, when the corporation has accepted subscriptions in excess of the capital stock, are not warranted in buying in shares of the stock at a discount on their own private account, and then re-issuing them at par in their capacity as officers, to provide for the oversubscription, charging the corporation par for the stock bought in, and thereby realizing a profit to themselves individually on the transaction. East New York, &c., R. R. Co. v. Elmore, 5 Hun, 214 (1875). Cf. Perkins v. Savage, 15 Wend. 412 (1836).

⁵ McClelland v. Whiteley, 11 Biss. 444 (1883); New Hampshire, &c., R. R. Co. v. Johnson, 30 N. H. 390 (1855).

these capacities.¹ And so also it is said that the commissioners' books are *prima facie* evidence of the subscriptions found in them,² and likewise as to the original subscription paper.³ And again, that entries in the proper books by commissioners duly appointed to take subscriptions, are evidence against the subscribers.⁴ So corporate books to which a subscription has been transferred by authority of the subscriber are evidence of the subscription,⁵ and also the books that contain the original subscriptions.⁶ But the presumption that one is a stockholder arising from the fact of his name being found in the stock and transfer book, is a disputable one, and the books are impeached and the presumption rebutted, if evidence is given that the alleged subscriber never accepted, but wholly refused to accept any stock from the company, which is to say that one who never accepts, but constantly refuses to accept stock in a corporation, is not proved to be a stockholder, by showing that the secretary of the company had entered his name as such in the books of the company.⁷ But when the books of the corporation have been destroyed or lost, a certified copy of the recorded list of the names of shareholders, required by statute to be filed in the office of the register of deeds, is *prima facie* evidence as to the fact of subscription and ownership of the shares.⁸ So it is said that the stock-book of a cor-

¹ Hoagland v. Bell, 36 Barb. 57 (1861); Turnbull v. Payson, 95 U. S. 418 (1877); Hamilton, &c., Co. v. Rice, 7 Barb. 157, 162 (1849); Pittsburgh, &c., R. R. Co. v. Applegate, 21 West Va. 172 (1882); Hoare's Case, 2 John. & H. 229 (1862); Taylor v. Hughes, 2 Jones & Lat. (Irish Chan.), 24, 55 (1844); McHose v. Wheeler, 45 Penn. St. 32 (1863). Cf. Coffin v. Collins, 17 Me. 440 (1840); Whitman v. Proprietors, &c., 24 Id. 236 (1844); Rockville, &c., Co. v. Van Ness, 2 Cranch C. C. 449 (1824); Mudgett v. Horrell, 33 Cal. 25 (1867), or when a certificate has been issued to him which he produces. Boardman v. Lake Shore, &c., R. R. Co. 84 N. Y. 157 (1881); Agricultural Bank v. Burr, 24 Me. 256.

² Rockwell, &c., Co. v. Van Ness, 2 Cranch C. C. 449 (1824); Wood v. Coosa, &c., R. R. Co., 32 Ga. 273 (1861).

³ Partridge v. Badger, 25 Barb. 146 (1857).

⁴ Wood v. Coosa, &c., R. R. Co., 32 Ga. 273 (1861).

⁵ Iowa, &c., R. R. Co. v. Perkins, 28

Iowa, 281 (1869); Hawley v. Upton, 102 U. S. 314 (1880). Cf. Whitman v. Proprietors, &c., 24 Me. 236 (1844).

⁶ Marlborough, &c., R. R. Co. v. Arnold, 9 Gray, 157 (1857). Cf. Mudgett v. Horrell, 33 Cal. 25 (1867).

⁷ Mudgett v. Horrell, 33 Cal. 25 (1867). Cf. Brewers, &c., Ins. Co. v. Burger, 10 Hun, 56 (1877). Where there is no law authorizing a paper containing the subscriptions to the capital stock of a corporation, to be filed in the office of the secretary of State, a copy thereof, certified under the seal of the secretary of State, is not admissible as evidence in a suit by the corporation, to charge the defendant as a stockholder. Troy, &c., R. R. Co. v. Kurr, 17 Barb. 581 (1854); Jackson v. Leggett, 7 Wend. 377 (1831); Tilsbury, &c., Co. v. Goodrich, 8 Ontario (Q. B. Div.), 565 (1885). Cf. Bouchaud v. Dias, 3 Denio, 238 (1846); Dick v. Balch, 8 Peters, 30 (1834).

⁸ Cleveland v. Burnham, 55 Wis. 598; s. c. 10 Am. & Eng. Corp. Cases, 221 (1885).

poration is not admissible in evidence in an action by a creditor of the corporation against one claimed to be a stockholder for the purpose of proving that he is such stockholder.¹ In general, the contract of subscription must be in writing, and cannot be established by parol,² and in order to let in secondary evidence, there must be proof of an original subscription and of the loss of the book or paper, or the absence of the original paper satisfactorily accounted for.³ But parol evidence is admissible to show that a certificate has been issued to one by a wrong Christian name.⁴ The mere erasure of a subscription will not of itself prevent a recovery upon it.⁵

§ 74. *Liability of the corporation for refusal to issue certificate of stock.*—A subscriber for shares of stock, in case the contract of subscription were regularly entered into, may, if the corporation refuse to issue him a certificate, have his action in equity for specific performance,⁶ or he may recover of the corporation in assumpsit, the value of the shares at the time of the demand.⁷ In case the full capital stock have been issued, then, of course, specific performance of an agreement to issue more shares cannot be had.⁸ The liability of a corporation to issue

¹ *Mudgett v. Horrell*, 33 Cal. 25 (1867). Where one enters his name in the personal memorandum-book of the president of a stock company, with the amount and number of shares which he has proposed to take upon the happening of a certain contingency which will put him in funds, which book at the time was merely a pocket memorandum, and had nothing about it to show that it was to contain a list of subscribers to the stock of the proposed company, such an entry is not evidence of a subscription for stock. *McClelland v. Whiteley*, 11 Biss. 444 (1883).

² *Vreeland v. New Jersey, &c., Co.*, 29 N. J. Eq. 188 (1878); *Pittsburgh, &c., R. R. Co. v. Gazzam*, 32 Penn. St. 340 (1858); *New Hampshire, &c., R. R. Co. v. Johnson*, 30 N. H. 390 (1855). See also § 52.

³ *Pittsburgh, &c., R. R. Co. v. Gazzam*, 32 Penn. St. 340 (1858); *Graff v. Pittsburgh, &c., R. R. Co.*, 31 Id. 489 (1858); *Johnson v. Wabash, &c., Co.*, 16 Ind. 389 (1861). Cf. *Hays v. Pittsburgh, &c., R. R. Co.*, 38 Penn. St. 81 (1860); *Pittsburgh, &c., R. R. Co. v. Clarke*, 29 Id. 146 (1857); *Fairfield, &c., Co. v. Thorp*, 13 Conn. 173 (1839); *Iowa, &c., R. R. Co. v. Perkins*, 28 Iowa, 281 (1869); *Cleveland v. Burn-*

ham, 55 Wis. 598; s. c. 10 Am. & Eng. Corp. Cases, 221.

⁴ *Cleveland v. Burnham*, 55 Wis. 598.

⁵ *Johnson v. Wabash, &c., Co.*, 16 Ind. 399 (1861). Cf. *Jewell v. Rock River, &c., Co.*, 101 Ill. 57 (1881); *Greer v. Chartiers R. R. Co.*, 96 Penn. St. 391 (1880); *Railroad Co. v. White*, 10 S. C. 155 (1878); *Burt v. Farrar*, 24 Barb. 518 (1857); *Ryder v. Alton, &c., R. R. Co.*, 13 Ill. 516 (1851).

⁶ *Ferguson v. Wilson, L. R.*, 2 Chan. 77 (1866).

⁷ *Wyman v. American Powder Co.*, 8 Cush. 168 (1851). But to entitle one to recover back money advanced to a corporation for shares, upon the grounds of a failure to issue the certificate, the subscriber must, before suit, rescind the contract and demand the money. *Swazy v. Choate, &c., Co.*, 48 N. H. 200 (1868).

⁸ *Finley, &c., Co. v. Kurtz*, 34 Mich. 89 (1876). For the refusal of the corporation to issue original stock to a subscriber, the measure of damages is the difference between the price contracted for and the market value on the day when the issue ought to have been made. *Van Allen v. Illinois, &c., R. R. Co.*, 7 Bosw.

stock to the subscribers thereof, does not necessarily devolve upon another corporation which succeeds to its debts, liabilities, and franchises.¹ In England, it seems that directors are not individually liable to subscribers for the breach by the corporation of its agreement to issue stock.²

§ 75. *Substitution of stockholders before the issue of the stock.*

—It is clear that a subscription to the capital stock of a company about to be incorporated, when regularly entered on the books of the commissioners, cannot be rescinded at the pleasure of the subscriber, and it seems to be the rule that a substitution of one subscriber for another can be effected, if at all, only by the erasure of the name of the original subscriber with the consent of the commissioners, and the substitution of another name. Until the substitution in this way, the original subscriber is not released.³ The corporation is not bound to issue a certificate of stock to a

515 (1861). For another rule as the measure of damages, and one more in favor of the plaintiff, see *Baltimore, &c., Ry. Co. v. Sewall*, 35 Md. 238 (1871), and see Chapter on Conversion and Measure of Damages. In Louisiana the universal legatee may pay for, and demand, the certificate of stock subscribed for by his ancestor. The executor has no power to cancel the subscription, and the stock cannot be appropriated by a subsequent subscriber, who subscribed for it by consent of the executor. *State v. Crescent City, &c., Co.*, 24 La. Ann. 318 (1872). Cf. *Wallace v. Townsend*, 43 Ohio, 537. If a mistake has been made by which the certificates and stock have been issued to the wrong person, a court of equity will remedy it. *O'Meara v. North Am. Min. Nev.*, 2 Nev. 112 (1866).

¹ *Conant v. National, &c., Co.*, 8 Jones & S. (N. Y. Super. Ct.) 83 (1875).

² *Ferguson v. Wilson*, L. R., 2 Chan. 77 (1866). But see also *Swift v. Jewsbury*, L. R., 9 Q. B. 301; *Betts v. De Vitre*, L. R., 3 Chan. 429, 441 (1868); *Henderson v. Lacon*, L. R., 5 Eq. 249 (1867); *Eaglesfield v. Marquis of Londonderry*, 25 Week. Rep. 190. In this country, directors are liable for improperly refusing to receive subscriptions to the capital stock. *Union Bank v. McDonough*, 5 La. 63 (1833).

³ *Ryder v. Alton, &c., R. R. Co.*, 13 Ill. 516 (1851). In this case, p. 521, the court says: "Conceding for the purposes

of this case, the power of the commissioners to permit one person to be substituted as a subscriber in the place of another, it does not appear from this plea that any such arrangement was consummated. The plea simply alleges that the defendant refused to return the thirty shares of stock, that G. agreed to take them, and that the commissioners counted them as belonging to the latter. This does not show either that the defendant ceased to be a subscriber or that G. then became one. It fails to show a legal discharge of the one, or a binding assumption by the other. The intended agreement was left incomplete and unconcluded. The agreement between the defendant and G. remained unexecuted. The signature of the defendant should have been erased from the books of subscription, and that of G. inserted in its place. It ought to appear from the plea that G. could be made liable to the corporation as an original subscriber for the stock. But the facts set forth in the plea would not be sufficient to charge him as a subscriber. If he cannot be held liable as such, the defendant is still responsible on his subscription. The latter had no right to rescind his contract at pleasure, and he yet continues liable thereon, unless he has been legally absolved from its performance." See also *Hawley v. Upton*, 102 U. S. 314 (1880); *Selma, &c., R. R. Co. v. Tipton*, 5 Ala. 787 (1843).

transferee in such a case.¹ The subscriber to the stock of a corporation may transfer his interest therein although the company is not yet incorporated. It has been held, however, that the corporation is not obliged to recognize as a stockholder such a vendee of the stock.² If, however, the vendor afterwards obtains the certificates and sells them again to others, he is liable to the first person to whom he sold his interest,³ and is liable also to the latter if the corporation is never formed.⁴ If the corporation is duly formed, the vendor may compel the vendee to pay for the subscription transferred.⁵

§ 76. *Right to recover back money advanced on shares upon a failure to organize the company.*—Where one has advanced money, in good faith, to the promoters of a company, as a deposit or assessment upon shares subscribed for to be subsequently issued, and the enterprise contemplated by the proposed incorporation is abandoned, or the company for any reason fails to be

¹ It is held in California, that where the owners of a mining claim agreed to incorporate themselves, and to take stock in the corporation in proportion to the interest of each in the mine, and, before the incorporation one of them transfers to a third person his right to the stock when issued, and gives him a certificate to that effect, the company after incorporation is not bound by the pretended transfer or certificate, and cannot be compelled to issue the stock to such a third person. *Hawkins v. Mansfield, &c., Co.*, 52 Cal. 513 (1877); *Morrison v. Gold Mountain, &c., Co.*, 52 Id. 306 (1877). But in Louisiana the company may be compelled to issue a certificate to one who acquires his interest by the death of the original subscriber. *State v. Crescent City, &c., Co.*, 24 La. Ann. 318. In Ohio, death revokes an agreement or offer to subscribe for stock. *Wallace v. Townsend*, 43 Ohio, 537 (1885). And in Maryland, the ground is broadly taken that the rights of an assignee in such a case, do not differ in principle in any respect from those of an ordinary assignee of stock after incorporation, and that, where the owners of certain passenger railway franchises in the city of Baltimore, entered into articles of association, in contemplation of incorporation, wherein it was provided, *inter alia*, that the beneficial interests in the properties, rights, and franchises of the association should be divided into a fixed

number of shares of a certain par value, transferable only on the books of the company, and one of such associates assigned certain of his shares, in the proposed corporation, before the incorporation, the assignees might maintain, in their own names, actions against the company, for damages for the refusal to issue the certificates, and that the measure of damages was the value of the stock at the time of the demand, together with the dividends accrued thereon at that time, with interest to the day of the trial. *Baltimore, &c., Ry. Co. v. Sewell*, 35 Md. 238 (1871), also *Merrimac, &c., Co. v. Levy*, 54 Penn. St. 227 (1867).

² *Hawkins v. Mansfield Gold Mining Co.*, 52 Cal. 513 (1877); *Morrison v. Gold Mountain G. M. Co.*, 52 Cal. 306; *Coleman v. Spencer*, 5 Blackf. (Md.) 197 (1839). *Contra*, *Baltimore City Ry. Co. v. Sewell*, 35 Md. 238 (1871); *Tempist v. Kilmer*, 3 C. B. 249 (1846); *Hunt v. Gunn*, 13 C. B. (N. S.) 226 (1862). See also *Chater v. San Francisco S. F. Co.*, 19 Cal. 219 (1861).

³ *Beckett v. Bilbraugh*, 8 Hare, 188 (1850).

⁴ *Kempson v. Saunders*, 4 Bing. 5. (1826). But the latter is not liable to take the shares nor to indemnify his vendor. *Jackson v. Cocker*, 4 Beav. 59 (1841).

⁵ *Mahan v. Wood*, 44 Cal. 462 (1872). And may collect a note given in payment.

incorporated, such subscriber may recover back the money so advanced.¹ Nor is he obliged to submit to the deduction of any part thereof to be applied to the payment of the expenses incurred by the promoters in attempting the incorporation.²

¹ *Nockels v. Crosby*, 2 Barn. & C. 814 (1825); *Kempson v. Saunders*, 4 Bing. 5; *Ward v. Lord Londesborough*, 12 C. B. 252 (1854); *Asphitel v. Sercombe*, 5 Exch. 147 (1850); *Williams v. Salmond*, 2 Kay & J. 463 (1856); *Chaplin v. Clarke*, 4 Exch. 403 (1849). *Cf.* *Vallans v. Fletcher*, 1 Exch. 20 (1847); *Grand Trunk, &c., Ry. Co. v. Brodie*, 9 Hare, 823 (1852).

And see also *Williams v. Page*, 24 Beav. 654 (1857). "A bill in equity lies to recover back money paid on a bubble." *Colt v. Woollaston*, 2 P. Wms. 154 (1723); *Green v. Barrett*, 1 Sim. 45 (1826). See also "the bubble act," 6 Geo. I, chap. 18.

² *Nockels v. Crosby*, *supra*. But see *contra*, *Williams v. Salmond*, *supra*.

CHAPTER V.

CONDITIONAL SUBSCRIPTIONS.

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| <p>§ 77. Definition.
78. Conditions subsequent.
79. Conditional subscriptions before incorporation.
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81. Parol conditions are void.
82. Conditional subscriptions after incorporation.</p> | <p>§ 83. What may be the condition.
84. Acceptance of the subscription by the corporation.
85. Construction of the condition.
86-87. Performance of the condition.
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89. Notice and calls on conditional subscriptions.</p> |
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§ 77. *Definition of conditional subscription.*—A conditional subscription is one in which payment can be enforced by the corporation only after the occurrence or after the performance by the corporation of certain things specified in the subscription itself.¹ Oral agreements made with the subscriber to the effect that payment will not be required except upon certain events or contingencies, are sometimes spoken of as conditions to the subscription, but more properly, are mere variations of a written contract, and are treated elsewhere.²

§ 78. *Conditions precedent and conditions subsequent.*—A conditional subscription is also to be distinguished from a subscription on a condition subsequent. A subscription on a condition subsequent contains a contract between the corporation and the subscriber, whereby the corporation agrees to do some act, thereby combining two contracts, one the contract of subscription, the other an ordinary contract of the corporation to perform certain specified acts.³ The subscription is valid and enforceable,

¹ A conditional subscription has often been spoken of as "a continuing offer, which is final and absolute when accepted." *Taggart v. Western Md. R. R. Co.*, 24 Md. 563 (1866); *Ashtabula & New London R. R. Co. v. Smith*, 15 Ohio St. 328 (1864); *Lowe v. Edgefield & K. R. R. Co.*, 1 Head (Tenn.), 659 (1858).

² See Chapter IX.

³ Thus, adding to a subscription the words "to be expended between the Connecticut river and the east line of the State," has been held to form a contract

to that effect, but not to make the subscription conditional. *Lane v. Brainerd*, 30 Conn. 565 (1862); *Henderson & Nashville R. R. Co. v. Leavell*, 16 B. Monroe (Ky.), 358 (1855). So also of words requiring a certain location or route to be adopted. *Henderson & Nashville R. R. Co. v. Leavell*, *supra*, the court saying, however, that if the route is laid out otherwise, before payment, probably the subscriber would be discharged; if changed after payment, it could be enjoined. Laches will bar the right to such an in-

whether the conditions are performed or not.¹ The condition subsequent is the same as a separate collateral contract between the corporation and the subscriber, for breach of which an action for damages is the remedy.² The distinction between such a contract and the ordinary conditional subscriptions, that is, subscriptions on conditions precedent, is sometimes difficult to determine. The Supreme Court of Maine has said that the question, whether a condition in a subscription "be precedent or subsequent, is a question purely of intent, and the intention must be determined by considering not only the words of the particular clause, but also the language of the whole contract, as well as the nature of the act required and the subject-matter to which it relates."³ The courts, in accordance with well established rules, favor conditions subsequent.⁴

junction. *Chapman v. Mad River & Lake Erie R. R. Co.*, 6 Ohio St. 119 (1856). A more frequent requirement is a certain location of the route, and also the construction of a part or the whole of the road. The first requirement is construed to be a condition precedent; the second a condition subsequent, since the payment of the subscription itself is necessary to carry out the requirement. *Chamberlain v. Painesville & Hudson R. R. Co.*, 15 Ohio St. 225 (1864); *Belfast & Moosehead Lake Ry. Co. v. Moore*, 60 Me. 561, 576 (1871); *North Mo. R. R. Co. v. Winkler*, 29 Mo. 318; *Bucksport & Bangor R. R. Co. v. Inhabitants of Bremer*, 67 Me. 295 (1877); *McMillan v. Maysville & Lexington R. R. Co.*, 15 B. Monroe, 218 (1854); *Swartout v. Mich. Air Line R. R. Co.*, 24 Mich. 389 (1872), where Judge Cooley says: "It is only reasonable to infer that they would have expressed that intent more clearly, and would have indicated with definiteness what stage the work should reach before their liability should become fixed." So also in *Miller v. Pittsburgh & Connellsville R. R. Co.*, 40 Pa. St. 237 (1861); where the court says: "It is a most extraordinary defense, for it presupposes that the company were to build their road without money, and to deliver it, a finished work, to the stock subscribers, who were then to pay their subscriptions. In *Pittsburgh & Steubenville R. R. Co. v. Biggar*, 34 Pa. St. 455 (1859), a condition "provided the road goes within half a mile of Florence," was held to be a condition subsequent. A condition that alterations shall be ordered only by a vote of the directors is a condition subsequent.

Bucksport & Bangor R. R. Co. v. Buck, 68 Me. 81 (1878). So also of a condition that commissioners should be appointed to see that other conditions are complied with. *Shaffner v. Jeffries*, 18 Mo. 512 (1853); and a condition that the money subscribed shall be expended on a certain part of the road. *Lane v. Brainerd*, 30 Conn. 565 (1862). For the English cases on conditions precedent and subsequent to subscriptions for stock, see Ch. II, § 18, n. 3.

¹ A condition subsequent "will not defeat an action for the recovery of the money, notwithstanding it had not been performed when the action was commenced." *Belfast & Moosehead Lake Ry. Co. v. Moore*, 60 Me. 561, 576 (1871). "A failure to perform an independent stipulation, not amounting to a condition precedent, though it subject the party failing to damages, does not excuse the party on the other side from the performance of all stipulations on his part." *Mill Dam Foundry v. Hovey*, 38 Mass. 417, 437 (1839).

² The subscriber is left to the ordinary remedies for breaches of contracts.

³ *Bucksport & B. R. R. Co. v. Inhabitants of Bremer*, 67 Me. 295 (1877). "The situation and relation of the parties to each other, the object sought to be attained, and the subject-matter to which the agreement relates, are material . . . and indispensable aids" in deciding whether the condition be precedent or subsequent. *Chamberlain v. Painesville & Hudson R. R. Co.*, 15 Ohio St. 225 (1864).

⁴ *Chamberlain v. Painesville & Hudson R. R. Co.*, 15 Ohio St. 225 (1864); *Swart-*

§ 79. *Conditional subscriptions not allowed in subscriptions to obtain incorporation.*—Conditional subscriptions made before the incorporation of a company, and taken for the purpose of securing such incorporation, as prescribed by statute, are of doubtful validity. The weight of authority holds that subscriptions taken for the purpose of complying with a statute which grants a charter only upon a certain amount of stock being subscribed, cannot be conditional, but must be absolute.¹ This is clearly the rule in New York and Pennsylvania, and is founded in justice, since only thus should a charter be granted to a corporation.²

§ 80. *In New York the subscription is void, in Pennsylvania the condition is void.*—The New York and Pennsylvania cases differ, however, in regard to the effect of a conditional subscription to stock before, and for the purpose of incorporation. In New York the whole subscription is void absolutely. It is as though not made, and cannot be enforced, either by the corporation, or by the would be subscriber.³ In Pennsylvania a different rule prevails. The condition is void, but the subscription itself is treated as an absolute unconditional subscription, and may be enforced by the corporation.⁴ The commissioners are held to have only limited

out *v. Mich. Air Line R. R. Co.*, 24 Mich. 389 (1872).

¹ "A subscription to the stock of a public corporation, made before letters patent are issued and an organization effected, must be considered absolute and unqualified, and any condition attached thereto void. Commissioners have no authority to receive conditional subscriptions." *Boyd v. Peach Bottom Ry. Co.*, 90 Pa. St. 169 (1879). "Any other rule would lead to the procurement from the commonwealth of valuable charters without any absolute capital for their support, and thus give rise to a system of speculation and fraud which would be intolerable." *Caley v. Phila. & Chester County R. R. Co.*, 80 Pa. St. 363 (1876). In New York the only case of a conditional subscription made before incorporation seems to be that of *Troy & Boston R. R. Co. v. Tibbits*, 18 Barb. 297 (1854), where the conditions restricted the powers to "call," and also provided for the payment of interest on the amounts paid in on subscriptions. The decision goes farther than the facts require, when it says that the Railroad Laws of 1848, "confers no

power to make conditional subscriptions, and such a thing is contrary to public policy." That conditional subscriptions are not to be counted in ascertaining whether the whole capital stock has been subscribed, which must be shown before another absolute subscriber can be made liable, see Chapter X.

² Some of the old cases uphold conditional subscriptions made previous to and for the purpose of incorporation. *Chamberlain v. Painesville & Hudson R. R. Co.*, 15 O. St. 225 (1864). It is doubtful, however, whether any well considered case, under the present common general law allowing the incorporation of railroads, would sustain such a subscription. The weight of authority is decidedly in favor of absolute subscriptions.

³ *Troy & Boston R. R. Co. v. Tibbits*, 18 Barb. 297 (1854).

⁴ "Where one subscribes to the stock of a public corporation, prior to the procurement of its charter, such subscription is to be regarded as absolute and unqualified, and any condition attached thereto is void." *Caley v. Phila. & Chester Co. R. R. Co.*, 80 Pa. St. 363 (1876). "The subscrip-

statutory powers, of which the subscriber is bound to take notice, and then express powers do not give authority to the commissions to take conditional subscriptions. They have no right to vary the terms of the subscriptions, and any conditions are held to be void as a fraud upon the State, upon corporate creditors, and upon other subscribers.¹

§ 81. *Parol conditions are void.*—Under the general rule of evidence that a written agreement cannot be varied or added to by parol, it is not competent for a subscriber to stock to allege that he is but a conditional subscriber.² The condition must be inserted in the writing in order to be effectual. Where, however, the parol agreement or condition is made subsequently to the making of the contract, and upon a sufficient consideration, it has been upheld.³

§ 82. *Conditional subscriptions after incorporation are valid.*—A conditional subscription to stock taken and accepted by a corporation after its incorporation, is legal and valid by the common law of all the States. In Pennsylvania the legality of such conditional subscriptions is clearly declared and sustained.⁴ In New York also conditional subscriptions have been upheld,⁵

tion itself is valid and binding, and the condition null and void." *Boyd v. Peach Bottom Ry. Co.*, 90 Pa. St. 169 (1879). To the same effect see *Bedford R. R. Co. v. Bowser*, 48 Pa. St. 29 (1864); *Barrington v. Pittsburgh & Steubenville R. R. Co.*, 44 Pa. St. 358; *Pittsburgh & Steubenville R. R. Co. v. Biggar*, 34 Pa. St. 455 (1859); *Id. v. Woodrow*, 3 Phil. 271 (1858). The subscription itself, however, is not binding, if it is not reported by the commissioners and used to obtain the charter. *Ligonier Valley R. R. Co. v. Williams*, 35 Leg. Intel. 40 (1878). In the Federal courts, *Burke v. Smith*, 16 Wall. 390, 396 (1872), favors the Pennsylvania rule, while *Putnam v. City of New Albany*, 4 Biss. 365, 383 (1869), favors the New York rule. In both cases the opinions are *dicta*. See also *Ellison v. Mobile & O. R. R. Co.*, 36 Miss. 572 (1858).

¹ Same cases.

² See Chapter IX.

³ *Id.*

⁴ "It is no longer to be doubted that an incorporated company after it has obtained its letters patent and effected its

organization, may receive conditional subscriptions to its stock." *Pittsburgh & Connellsville R. R. Co. v. Stewart*, 41 Pa. St. 54 (1861); *Caley v. Phila. & Chester County R. R. Co.*, 80 Pa. St. 363 (1876). After incorporation conditional subscriptions may be received, although the letters patent have not been issued and cannot be until ten per cent. of the capital stock is subscribed. The conditional subscription cannot, however, form any part of such percentage. *Hanover Junction & Susquehanna R. R. Co. v. Haldeman*, 82 Pa. St. 36 (1876).

⁵ Ordinary conditional subscriptions were treated as being valid in *Union Hotel Co. v. Hersee*, 79 N. Y. 454 (1880); *Burrows v. Smith*, 10 N. Y. 550 (1853); *Morris Canal & Bkg. Co. v. Nathan*, 2 Hall, 239 (1829). But the condition that a particular location of the proposed road should be adopted has been held to be contrary to public policy, since improper means would thereby influence the question of location. *Butternuts & Oxford Turnpike Co. v. North*, 1 Hill, 518 (1841); *Fort Edward & Fort Miller Plank Road Co.*

but not where the condition is one that affects the route of a turn-pike or railroad company. In other States the legality of such subscriptions is rarely questioned, but is generally assumed to be admitted.¹

§ 83. *What condition may be attached to a subscription.*—

Any condition which can be legally performed or complied with by the corporation may be the condition to a subscription for stock.² The condition may be that payment shall be in labor or materials;³ it may require the expenditure of the subscription on a particular part of the enterprise;⁴ it may stipulate that a certain amount or the whole of the capital stock shall be subscribed before calls are made on the subscriptions;⁵ or it may limit the time within which certain things specified therein must be done.⁶ In most States the condition to a subscription may require the route of a railroad to be located on a particular line.⁷ In New

v. Payne, 15 N. Y. 583 (1857); *Macedon & Bristol Plank Road Co. v. Snediker*, 18 Barb. 317 (1854); *dictum* in *Dix v. Shaver*, 14 Hun, 392 (1878). However, in the case of *Lake Ontario Shore R. R. Co. v. Curtiss*, 80 N. Y. 219 (1880), a condition of this kind was involved, and no objection was made to its validity. Subscriptions conditional in the payment in property, labor, or contract for construction, have been repeatedly passed upon in New York and upheld. See Chapter II.

¹ "Except in New York, conditional subscriptions, in the absence of a special prohibition, so far as we have observed, have been sustained as authorized and not in conflict with public policy." *Ashtabula & New London R. R. Co. v. Smith*, 15 Ohio St. 328 (1864). See also *New Albany & Salem R. R. Co. v. McCormick*, 10 Ind. 499 (1858); *McMillan v. Maysville & Lexington R. R. Co.*, 15 B. Monroe, 218 (1854).

² The subscriber "may agree to take and pay for the stock absolutely or upon such conditions as he may choose to incorporate into his subscription." *Penobscot & Kennebec R. R. Co. v. Dunn*, 39 Me. 587 (1855).

³ See Chapter II.

⁴ *Milwaukee & Northern Ill. R. R. Co. v. Field*, 12 Wis. 340 (1860); *Hanover Junction & Sus. R. R. Co. v. Haldeman*, 82 Pa. St. 36 (1876).

⁵ *Phil. & West Chester R. R. Co. v. Hickman*, 28 Pa. St. 318; *Penobscot & Kennebec R. R. Co. v. Dunn*, 39 Me. 587

(1855); *Hanover Junction & Sus. R. R. Co. v. Haldeman*, *supra*; *Union Hotel Co. v. Hersee*, 79 N. Y. 454 (1880); upheld, although the charter allowed commencement of business upon the subscription of a less sum. *Ridgefield & N. Y. R. R. Co. v. Brush*, 43 Conn. 86 (1875).

⁶ *Ticonic Water Power & Mfg. Co. v. Lang*, 63 Me. 480 (1874), holding also that time herein is of the essence of the contract. See also *Morris Canal & Bkg. Co. v. Nathan*, 2 Hall (N. Y.), 239 (1829). See also § 87.

⁷ *Fisher v. Evansville, &c., R. R. Co.*, 7 Ind. 407 (1856); *Conn. & Passumpsic R. R. Co. v. Baxter*, 32 Vt. 805 (1860); *Umbertland Valley R. R. Co. v. Baab*, 9 Watts, 458 (1840); *Evansville, &c., R. R. Co. v. Sharer*, 10 Ind. 246 (1858); *Jewett v. Lawrenceburgh, &c., R. R. Co.*, 10 Ind. 539 (1858); *Missouri Pacific Ry. Co. v. Taggard*, 84 Mo. 264 (1884); *Wear v. Jacksonville, &c., R. R. Co.*, 24 Ill. 595 (1860); *Taggart v. Western Md. R. R. Co.*, 24 Md. 563 (1866); *Racine County Bk. v. Ayers*, 12 Wis. 512 (1860). See also *Caley v. Phil. & Chester County R. R. Co.*, 80 Pa. St. 363 (1876). Location may be required to be subject to the approval of the subscriber. *Roberts' Case*, 3 De Gex & Sm. 205 (1850); *aff'd*, 2 Mac. & G. 196. See also *Mansfield, &c., R. R. Co. v. Brown*, 26 Ohio St. 224 (1875); *Id. v. Stout*, 26 Ohio St. 241 (1875); *Chamberlain v. Painesville, &c., R. R. Co.*, 15 Ohio St. 225 (1864); *North, &c., R. R. Co. v. Winkler*, 29 Mo. 318 (1860); *Spartan-*

York such a conditional subscription has been held to be void, on the ground of public policy, inasmuch as the discretion of the directors, in laying out the route, would thereby be influenced by considerations other than those of a purely public nature.¹

In general, however, subscriptions to the capital stock of a corporation may be conditional as to the time, manner, or means of payment, or in any other way not prohibited by statute, or the rules of public policy, and not beyond the corporate powers of the corporation to comply with.²

§ 84. *Acceptance by the corporation is necessary.*—The acceptance by the corporation of a conditional subscription is necessary to the formation of the contract.³ Until such acceptance, the conditional subscription is but a continuing offer. After acceptance, the subscriber is bound, until performance of the condition by the corporation, to await such performance; he cannot withdraw the conditional subscription after it has been accepted. It seems, however, that if the performance of the condition is delayed unreasonably by the corporation, the conditional subscriber will be thereby released from his obligation.⁴

burgh, &c., R. R. Co. v. Greffensied, 12 Rich. L. 675 (1860); Des Moines, &c., R. R. Co. v. Graff, 27 Iowa, 99 (1869). A subscription or note, not for stock but absolutely as a gift, to the corporation, in consideration of a particular route being adopted, has been upheld. Stowell v. Stowell, 45 Mich. 364; First Natl. Bk. v. Hendrie, 49 Iowa, 402 (1878). *Contra*, Holaday v. Patterson, 5 Oreg. 177 (1874).

¹ See § 52.

² Conditions inconsistent with the charter are void. Thigpen v. Miss., &c., R. R. Co., 32 Miss. 347 (1856). The conditions which may be legally made to a subscription are practically limited only by the power of the corporation to contract. A few of the conditions which have been passed upon by the courts have been given. Many minor ones are involved in the cases, and present a great variety of conditions, corresponding as they do to the wishes and motives of individuals subscribing to the stock of the different kinds of joint-stock corporations.

³ Junction R. R. Co. v. Reeve, 15 Ind. 236 (1860), where the subscription was payable in land. See also Galt's Ex'rs v. Swain, 9 Gratt. (Va.) 633 (1853).

"When the offer was accepted, the minds of the parties met and the contract was complete. . . . The acceptance by the plaintiff constituted a sufficient legal consideration for the engagement on the part of the defendants." Taggart v. Western Md. R. R. Co., 24 Md. 563 (1866). By the entry of the subscription on the corporate record, an acceptance is implied. New Albany & Salem R. R. Co. v. McCormick, 10 Ind. 499 (1858). Acceptance by the president of the corporation, and a subsequent ratification by the directors of all his acts, is sufficient. Pittsburgh & Connellsville R. R. Co. v. Stewart, 41 Pa. St. 54 (1861). The delivery and acceptance may be proved by parol. Mansfield & New Lisbon R. R. Co. v. Smith, 15 O. St. 328 (1864). Where it is delivered in escrow to the agent of the corporation, there can be no acceptance of it by the corporation, so long as such delivery continues. Cass v. Pittsburgh, Va. & Charleston Ry. Co., 80 Pa. St. 31 (1875). It may be revoked while still in the hands of a corporate agent. Lowe v. Edgefield & K. R. R. Co., 1 Head (Tenn.), 659 (1858.)

⁴ "The objection to a continuing offer, that it suspends indefinitely the liability

§ 85. *Construction of conditional subscriptions.*—Conditional subscriptions, like other contracts, are to be construed reasonably and according to the intent of the parties, as indicated by the language used in the contract.¹ The circumstances under which the subscription was made are also to be taken into consideration.² If two interpretations are possible, that which facilitates the enterprise is preferred to that which retards it.³ If the meaning is ambiguous, it is for the jury to say what the interpretation is to be.⁴

§ 86. *Performance of the condition.*—A condition to a subscription for stock must be performed or complied with before the subscriber can be compelled to pay such subscription.⁵ A substantial performance of the condition is sufficient.⁶ A failure to perform is not excused by reason of unforeseen difficulties arising from floods and natural causes.⁷ A conditional subscriber is not a stockholder or member of the corporation until after the

of the conditional subscribers is sufficiently answered by the consideration that all such offers are subject to retraction, and may be recalled if their acceptance is unreasonably deferred." *Taggart v. Western Md. R. R. Co.*, 24 Md. 563 (1866). See query and briefs in *Mansfield, Coldwater & Lake Mich. R. R. Co. v. Stout*, 26 O. St. 241 (1875), which holds that the question of acceptance is immaterial where performance of the condition has been completed by the corporation.

¹ The whole contract is to be taken together, and is "to have a reasonable construction according to the intent of the parties." *People's Ferry Co. v. Balch*, 74 Mass. 303 (1857). "The language was chosen by them to express their mutual intent, and such construction must be given thereto as will carry into effect that mutual understanding. . . . We are to ascertain what the parties understood and intended by this language, and may not deviate therefrom, whether that contract, as so interpreted, be wise or unwise for either party." *Memphis, Kan. & Col. R. R. Co. v. Thompson*, 24 Kan. 170 (1880).

² "The contract must be interpreted by the light of the circumstances which existed at the time it was made, and not of those which arose afterwards." *Monadnock R. R. v. Felt*, 52 N. H. 379 (1872); *Detroit L. & L. M. R. R. Co. v. Starnes*, 38 Mich. 698 (1878).

³ *Ashtabula & New Lisbon R. R. Co. v. Smith*, 15 O. St. 328 (1864). See also § 51.

⁴ *Connecticut R. R. Co. v. Baxter*, 32 Vt. 805 (1860).

⁵ *Porter v. Raymond*, 53 N. H. 519 (1873); *Monadnock R. R. v. Felt*, 52 N. H. 379 (1872); *Montpelier & Wells River R. R. Co. v. Langdon*, 46 Vt. 284 (1873); *Ashtabula & New Lisbon R. R. Co. v. Smith*, 15 O. St. 328 (1864); *Phil. & West Chester R. R. Co. v. Hickman*, 28 Pa. St. 318 (1857); *Burrows v. Smith*, 10 N. Y. 550. "Upon the performance of the condition by the promisee, the contract is clothed with a valid consideration, which relates back, and the promise at once becomes obligatory." *Des Moines Valley R. R. Co. v. Graff*, 27 Iowa, 99 (1869).

⁶ *O'Neal v. King*, 3 Jones' L. (N. C.) 517 (1856). See also *Virginia, &c., R. R. Co. v. County Comm'rs, &c.*, 8 Nev. 68 (1870); *Springfield St. Ry. Co. v. Sleeper*, 121 Mass. 29 (1876); *People v. Holden*, 82 Ill. 93 (1876). Performance must be within a reasonable time. *Stevens v. Corbitt*, 33 Mich. 458 (1876). In the case of *Martin v. Pensacola & Geo. R. R. Co.*, 8 Fla. 370, 390 (1869), it is stated in a *dictum*, that a strict compliance is necessary.

⁷ *Memphis, Kan. & Col. R. R. Co. v. Thompson*, 24 Kan. 170 (1880).

condition is performed.¹ Whether or not the condition has been performed is a question of fact.² Performance may be proved by parol or by the records of the corporation.³

§ 87. Where the condition is that the work shall be begun, contracted for, or completed within a certain time, time is of the essence of the contract, and any failure to perform within the time so specified, defeats the subscription.⁴ A condition that the road shall be "permanently" located on a specified route is satisfied by the adoption of that route by the directors.⁵ Where the question of whether performance has been completed, rests in the decision of the directors, their conclusion cannot be questioned, unless fraud or bad faith is proved.⁶ A condition that the subscription shall be applied to a particular portion of the road is satisfied by the completion of that portion.⁷ Any fraud on the part of the corporation in the performance of the condition may be shown by parol.⁸ All of several conditions must be performed before calls are made.⁹ But if one part of the subscrip-

¹ *Chase v. Sycamore & Courtland R. R. Co.*, 38 Ill. 215 (1865); *Slipher v. Earhart, Adm.*, 83 Ind. 173 (1882); *Evansville, Ind. & Cleveland S. L. R. R. Co. v. Shearer*, 10 Ind. 244 (1858).

² *Jewett v. Lawrenceburgh & U. M. R. R. Co.*, 10 Ind. 539 (1858). And is a question for the jury. *St. Louis & Cedar Rapids R. R. Co. v. Eakins*, 30 Iowa, 279 (1870).

³ By parol. *St. Louis & Cedar Rapids R. R. Co. v. Eakins*, 30 Iowa, 279 (1870). By corporate records, *Penobscot & Kennebec R. R. Co. v. Dunn*, 39 Me. 587 (1855). *Contra*, *Phil. & West Chester R. R. Co. v. Hickman*, 28 Pa. St. 318 (1857). Performance must be alleged in the complaint or declaration. *Trott v. Saschett*, 10 O. St. 241 (1859); *Roberts v. Mobile & O. R. R. Co.*, 32 Miss. 373 (1856); *Henderson & Nashville R. R. Co. v. Leavell*, 16 B. Monroe, 358 (1855).

⁴ *Burlington & Missouri River R. R. Co. v. Boestler*, 15 Iowa, 555 (1864), per Dillon, J.; *Freeman v. Mack*, 67 Ind. 99 (1879); *Memphis, Kan. & Col. R. R. Co. v. Thompson*, 24 Kan. 170 (1880); *Portland & Oxford Central R. R. Co. v. Inhabitants of Hartford*, 58 Me. 23 (1870). If the directors certify that the condition was performed within the specified time, the subscriber may prove

the falsity of their certificate. *Morris Canal & Bkg. Co. v. Nathan*, 2 Hall (N. Y.), 239 (1829). Upon the failure of the corporation to comply with this condition, the subscription ceases to have any vitality "by its own limitation." *Ticonic Water Power & Mfg. Co. v. Lang*, 63 Me. 480 (1874). In the case, however, of *Missouri Pacific Ry. Co. v. Taggard*, 84 Mo. 264 (1884), a completion of the road within a reasonable time after the time specified in the condition was held to be a substantial performance and sufficient, the grading having been completed in the specified time.

⁵ *Smith v. Allison*, 23 Ind. 366 (1864), and see cases in § 78. So also a condition that the road shall cross another at a certain point is satisfied by its being so located. *Wear v. Jacksonville & Savannah R. R. Co.*, 24 Ill. 593 (1860).

⁶ *Cass v. Pittsburg, Va. & Charleston Ry. Co.*, 80 Pa. St. 31 (1875), and see note 3.

⁷ *Nichols v. Burlington & Louisa County Plank Road Co.*, 4 Greene (Iowa), 42 (1853).

⁸ *New York Ex. Co. v. De Wolf*, 31 N. Y. 271 (1865).

⁹ *Porter v. Raymond*, 53 N. H. 519 (1873).

tion be free from condition, it may be collected independently.¹ Where after part payment by the conditional subscriber, the corporate plans are changed, so that the condition is not complied with, the money, it has been held, may be recovered back.²

§ 88. *Waiver of the condition.*—A conditional subscriber to the stock of a corporation may waive the condition and performance thereof, and thus become liable on his subscription, as though it had been originally an absolute one. The waiver may be by an oral statement or agreement of the subscriber.³ Certain acts of the subscriber have been held to indicate an intent to waive a condition to the subscription, and to be equivalent to a direct waiver. Thus acting as a director,⁴ or as president of the corporation,⁵ paying the whole of the subscription,⁶ giving an absolute promissory note without conditions in payment of the subscription⁷ have each been held to constitute a waiver of the condition to a subscription. But mere silence is not a waiver,⁸ nor payment of part of the subscription,⁹ nor aid in the attempt to start the enterprise, by soliciting subscriptions and being elected to a corporate office.¹⁰

§ 89. *Notice of performance and calls.*—There is some doubt as to whether, upon performance of the condition, the subscriber is entitled to notice of such performance. The better rule seems to be that he is entitled to such notice, and that a general "call" for the payment of part or all of the subscriptions for stock, does

¹ St. Louis, &c., R. R. Co. v. Eakins, 30 Iowa, 279 (1870).

² Jewett v. Lawrenceburg & U. M. R. R. Co., 10 Ind. 539 (1858).

³ Hanover Junction & Sus. R. R. Co. v. Haldeman, 82 Pa. St. 36 (1876). See also Woonsocket Union R. R. Co. v. Sherman, 8 R. I. 564 (1867).

⁴ Lane v. Brainerd, 30 Conn. 565 (1862).

⁵ Dayton & Cincinnati R. R. Co. v. Hatch, 1 Disney (O.), 84 (1855).

⁶ Parks v. Evansville, Ind. & Cleveland S. L. R. R. Co., 23 Ind. 567 (1864).

⁷ Chamberlain v. Painesville & Hudson R. R. Co., 15 O. St. 225 (1864); Slipper v. Earhart, Adm., 83 Ind. 173 (1882); Evansville, &c., R. R. Co. v. Dunn, 17 Ind. 603; Keller v. Johnson, 11

Ind. 337 (1858); O'Donald v. Evansville, &c., R. R. Co., 14 Ind. 259 (1860); but not where the note was given by reason of false representations that the condition had been complied with. Parker v. Thomas, 19 Ind. 213 (1862); Taylor v. Fletcher, 15 Ind. 80 (1860).

⁸ Burlington & Mo. River R. R. Co. v. Boestler, 15 Iowa, 555 (1864); Bucksport & Bangor R. R. Co. v. Inhabitants of Bremer, 67 Me. 295 (1877).

⁹ Pittsburgh & Connellsville R. R. Co. v. Stewart, 41 Pa. St. 54 (1861); Robert's Case, 2 Mac. & G. 196 (1850); Jewett v. Lawrenceburgh & U. M. R. R. Co., 10 Ind. 539 (1858).

¹⁰ Ridgefield & N. Y. R. R. Co. v. Reynolds, 46 Conn. 375 (1878).

not apply to conditional subscribers, unless the condition has been performed, and the fact of performance has been brought to the attention of the subscriber.¹

¹ Chase *v.* Sycamore & Courtland R. R. Co., 38 Ill. 215 (1865); Trott *v.* Sarchett, 10 O. St. 241 (1859). *Contra*, Nichols *v.* Burlington & Louisa County Plank Road Co., 4 Greene (Iowa), 42 (1853); Spartanburg & Union R. R. Co. *v.* De Graffenreid, 12 Rich. L. (S. C.) 675 (1860), holding that no "call" is necessary, and that interest runs from the time of performance. See Chap. II, as to calls, &c., when payment is in property.

CHAPTER VI.

MUNICIPAL SUBSCRIPTIONS.

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| <p>§ 90. A municipal corporation has no implied power or authority to subscribe for stock in any other corporation.</p> <p>91. The legislature may authorize municipal subscriptions to public, but not to private enterprises.</p> <p>92. Constitutional provisions prohibiting municipal subscriptions.</p> <p>93. Power to subscribe, how to be exercised.</p> <p>94. Submission to popular vote.</p> <p>95. What officer or agent of the municipality may make the contract of subscription.</p> <p>96. Formal requisites of a municipal subscription.</p> | <p>§ 97. Municipal subscriptions may be conditional.</p> <p>98. A municipal subscription may be paid in bonds instead of money.</p> <p>99. A municipal corporation as a stockholder.</p> <p>100. A municipality may enforce delivery of stock to itself in a proper case.</p> <p>101. Change in the State Constitution, or the general statutory laws, after the municipal corporation has voted to subscribe.</p> <p>102. Division of the municipality after the subscription.</p> <p>103. Consolidation of companies after the municipal aid is voted.</p> |
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§ 90. *A municipal corporation has no implied power or authority to subscribe for stock in any other corporation.*—A municipal corporation, being in its nature and purposes a very different legal institution from an ordinary private corporation, being indeed but a mode or department of government—"an investing the people of a place with the local government thereof"¹—it is plain that the general rules of law applicable to private corporations having capital stock are, for the most part, inapplicable when the rights, duties, powers, and liabilities of municipal corporations are sought to be accurately determined.²

It is proposed to consider the right of a municipality to enter into the contract of subscription to the capital stock of other corporations, and of the liabilities, rights, and duties growing out of such a subscription. The subject practically narrows itself to the right of municipal corporations to subscribe to the stock of railway corporations, inasmuch as this right, wherever it exists, is almost universally exercised in favor of these corporations, and

¹ Salk., 183; Taylor on Corp., § 315; Dillon on Munic. Corp., §§ 19, 20.

² People v. Morris, 13 Wend. 325 (1835); People v. Hurlburt, 24 Mich. 44;

State v. Leffingwell, 54 Mo. 458; Norton v. Peck, 4 Wis. 714; Ottawa v. Carey, 108 U. S. 110 (1883).

the adjudicated cases almost all present phases of the question as applying to them.

It is a well settled rule of law that municipal corporations have no implied right or authority to subscribe for the stock of any other incorporated company.¹ In order, therefore, to the validity of a municipal subscription to the stock of a railway company, an express grant of authority from the legislature must be shown.² The right to subscribe is derived from the legislative enactment, and whether or not an enabling act is sufficient to validate a subscription is a question of law for the court, not for the jury.³ The right to make a donation to a railroad or other work of internal improvement must equally be derived from the act of the legislature. Without such express authority of law a donation or issue of bonds as a gift to a railroad company is invalid and void.⁴

§ 91. *The legislature may authorize municipal subscriptions to public, but not to private enterprises.*—It was long a question whether the legislature had the constitutional right to authorize a municipality to subscribe money, or donate it, in furtherance of any enterprise not governmental in its nature. It has been

¹ "To become stockholders in private corporations," says Judge Dillon, "is manifestly foreign to the usual purposes intended to be subserved by the creation of corporate municipalities." Dillon on Munic. Corp., § 161; *Acc. Kenicott v. Supervisors*, 16 Wall. 452 (1872); *Thompson v. Lee County*, 3 Id. 327 (1865); *Bell v. Railroad Co.* 4 Id., 598 (1866); *Wells v. Supervisors*, 102 U. S. 625 (1880); *City of Lynchburg v. Slaughter*, 75 Va. 57; *Louisville, &c. R. R. Co. v. Fairfield*, 51 Vt. 257 (1878); *Barnes v. Lacon*, 84 Ill. 461 (1877); *Brodie v. McCabe*, 33 Ark. 690 (1878); *Pennsylvania R. R. Co. v. Philadelphia*, 47 Penn. St. 189 (1864); *City of Jonesboro' v. Cairo, &c. R. R. Co.*, 110 U. S. 192 (1883); *Gelpcke v. Dubuque*, 1 Wall. 220 (1863); *Campbell v. Paris, &c. R. R. Co.*, 71 Ill. 611 (1874); *East Oakland v. Skinner*, 94 U. S. 255 (1876). See also, for a full discussion of this question, Wood on Railways, § 100, and cases collected; *Taylor on Corp.*, §§ 316, 319, 320.

² *Sharpless v. The Mayor*, 21 Penn. St. 147 (1853); *Leavenworth Co. v. Miller*, 7 Kan. 479 (1871); s. o., 12 Am. Rep. 425; *Welch v. Post*, 99 Ill. 471 (1881); *Allen*

v. Louisiana, 103 U. S. 80 (1880); *Marsh v. Fulton Co.*, 10 Wall. 676 (1870); *La Fayette v. Cox*, 5 Ind. 38 (1854); *Commercial Bank v. Iola*, 2 Dillon, 363 (1873); *Dillon on Munic. Corp.*, § 161; *Wood on Railways*, § 100; *Ottawa v. Carey*, 108 U. S. 110 (1883); *Lewis v. City of Shreveport*, 108 Id. 282.

³ *Post v. Supervisors*, 105 U. S. 667 (1881). Moreover, every holder of municipal bonds issued to raise money to pay such a subscription, whether he receive them directly from the town or county, or from the railway company to which they may have been delivered, or takes them from some prior holder in the ordinary course of business, is chargeable with notice of the statutory provisions under which they were issued.

Ogden v. County of Daviess, 102 U. S. 634 (1880); *Lewis v. City of Shreveport*, 108 Id. 282 (1883); *City of Ottawa v. Carey*, 108 Id. 110 (1883); *McClure v. Township of Oxford*, 94 Id. 429 (1876). This is the settled rule of the Supreme Court of the United States on this point.

⁴ *Dixon County v. Field*, 111 U. S. 83 (1884).

very stoutly contended that such a right does not inhere in the legislative branch of the government in this country, and that in consequence such assumed grants are unconstitutional and void.¹ But it is now a reasonably well settled rule that the legislature has the constitutional power to authorize a municipal corporation by its charter or by an express act, to subscribe to the stock of railway or other *quasi* public corporation, and to issue and sell its bonds for that purpose.²

¹ Cooley on Const. Lim., pp. 261–266; Dillon on Munic. Corp., §§ 12, 117, 153.

This seems to be the rule in Michigan. *People v. Detroit*, 28 Mich. 228 (1873); *People v. Salem*, 20 Id. 452 (1870); *Thomas v. Port Hudson*, 27 Id. 320 (1873); *Bay City v. State Treasurer*, 23 Id. 499. But see *Talcott v. Pine Grove*, 1 Flippin, 120 (1871); *Township of Pine Grove v. Talcott*, 19 Wall. 666 (1873); *Taylor v. Ypsilanti*, 105 U. S. 60 (1881); *Chickaming v. Carpenter*, 106 U. S. 663 (1882).

"In Iowa, up to 1858, it was held that such acts were constitutional, but from that time up to 1869 they were held to be unconstitutional, when the court seems to have undergone a radical change, and from that time to the present the constitutionality of such measures has been sustained." Wood on Railways, p. 264, citing *Dubuque Co. v. Dubuque, &c. R. R. Co.*, 4 Greene (Iowa), 1 (1853); *State v. Bissell*, 4 Id. 328 (1854); *Clapp v. Cedar Co.*, 5 Iowa, 15 (1857); *McMillen v. Lee Co.*, 6 Id. 391 (1858). The above authorities, prior to 1858, hold these acts constitutional, as do the following, handed down since 1869: *Stewart v. Polk Co.*, 30 Iowa, 9 (1870); *McGregor v. Birdsall*, 32 Id. 149, 255; *Jordan v. Hayne*, 36 Id. 9 (1872); *Muscataine, &c. R. R. Co. v. Horton*, 38 Id. 33 (1873); *Wapello v. B. & M. R. R. Co.*, 44 Id. 585 (1876). While the following cases, decided between 1858 and 1869, hold such acts unconstitutional and void. *Stokes v. Scott*, 10 Iowa, 166 (1859); *State v. Wapello*, 13 Id. 388 (1862); *Myers v. Johnson*, 14 Id. 47 (1862).

In New York the courts have inclined to take ground against the validity of such grants. *Sweet v. Hurlburt*, 51 Barb. 312 (1868); *Clarke v. Rochester*, 28 N. Y. 605 (1864); *Grant v. Coortor*, 24 Barb. 232 (1857); *Benson v. Albany*, 24 Id. 248 (1857); *People v. Henshaw*, 61 Id. 409 (1870); *Ex parte Taxpayers of Kingston*, 40 How. Prac. 444 (1870); *People v.*

Batchellor, 53 N. Y. 128 (1873). *Cf. Queensburg v. Culver*, 19 Wall. 82 (1873), in which the New York doctrine is denied by the Supreme Court of the United States.

² So held by the Supreme Court of the United States. *Knox County v. Aspinwall*, 21 How. 539; *Zabriskie v. Railroad Co.*, 23 Id. 381; *Amey v. Mayor*, 24 Id. 365, 376; *Curtis v. Butler Co.*, 24 Id. 435; *Gelpcke v. Dubuque*, 1 Wall. 175 (1863); *Mercer Co. v. Hackett*, 1 Id. 81 (1863); *Seybert v. Pittsburgh*, 1 Id. 273 (1863); *Van Hastrup v. Madison*, 1 Id. 291 (1863); *Havemeyer v. Iowa Co.*, 3 Id. 294 (1865); *Thompson v. Lee County*, 3 Id. 327 (1865); *Rogers v. Burlington*, 3 Id. 654 (1865); *Mitchell v. Burlington*, 4 Id. 270 (1866); *Von Hoffman v. Quincy*, 4 Id. 535 (1866); *Campbell v. Kenosha*, 5 Id. 194 (1866); *Supervisors v. Schenck*, 5 Id. 772 (1866); *Meyer v. Muscatine*, 1 Id. 384 (1863); *Lee County v. Rogers*, 7 Id. 181 (1868); *Beloit v. Morgan*, 7 Id. 619 (1868); *City of Kenosha v. Lamson*, 9 Id. 477 (1869); *Railroad Co. v. County of Otoe*, 16 Id. 667 (1872); *s. c.*, 1 Dillon, 338; *Olcott v. Supervisors*, 16 Id. 678 (1872); *Rock Creek v. Strong*, 99 U. S. 271 (1877); *Hickory v. Ellery*, 103 Id. 423 (1880); *Clay Co. v. Society for Savings*, 104 Id. 579 (1881); *Taylor v. Ypsilanti*, 105 Id. 60 (1881); *Lewis v. Barbour Co.*, 105 Id. 739 (1881); *Amoskeag National Bank v. Ottawa*, 105 Id. 667 (1881); *Woods v. Lawrence Co.*, 1 Black. 380; *Gilman v. Sheboygan*, 2 Id. 510; *Town of Scipio v. Wright*, 101 U. S. 665 (1879); and in the Circuit and District Courts of the United States: *Long v. New London*, 9 Biss. 539 (1880); *Sibley v. Mobile*, 3 Woods, 535 (1876); *United States v. New Orleans*, 2 Id. 230 (1876).

Alabama—*Stein v. Mayor, &c.*, 24 Ala. 591 (1854); *Opelika v. Daniel*, 59 Ala. 211 (1877); *Ex parte Selma, &c. R. R. Co.*, 45 Id. 596 (1871); *Gibbons v. Mobile, &c. R. R. Co.*, 36 Id. 410 (1860).

Arkansas—*Mississippi, &c. R. R. Co.*

The act of the legislature authorizing a municipal subscrip-

v. Camden, 23 Ark. 300 (1861); *English v. Chicot Co.*, 26 Id. 455 (1871); *Jacksonport v. Watson*, 33 Id. 704 (1878).

California—*Robinson v. Bidwell*, 22 Cal. 379 (1863); *People v. Coon*, 25 Id. 635 (1864); *Napa Valley R. Co. v. Napa County*, 30 Id. 435 (1866); *Stockton, &c. R. R. Co. v. Stockton*, 41 Id. 147 (1871).

Colorado—*People v. Pueblo Co.*, 2 Col. 360 (1874).

Connecticut—*Bridgeport v. Housatonic R. R. Co.*, 15 Conn. 475 (1843); *Beardsley v. Smith*, 16 Id. 368 (1844); *Society, &c. v. New London*, 29 Id. 174 (1860); *Douglass v. Chatham*, 41 Id. 211 (1874).

Florida—*Cotton v. Leon Co.*, 6 Fla. 610 (1856).

Georgia—*Winn v. Macon*, 21 Ga. 275 (1857); *Powers v. Superior Court of Dougherty County*, 23 Id. 65 (1857).

Illinois—*Shaw v. Dennis*, 5 Gilm. 405; *Prettyman v. Tazewell Co.*, 19 Ill. 406 (1858); *Robertson v. Rockford*, 21 Id. 451 (1859); *Supervisors of Schuyler Co. v. People*, 25 Id. 181 (1860); *Butler v. Dunham*, 27 Id. 474 (1861); *Dunnovan v. Green*, 57 Id. 63 (1870); *Madison Co. v. People*, 58 Id. 456 (1871); *Chicago, &c. R. R. Co. v. Smith*, 62 Id. 268 (1871); *Decker v. Hughes*, 68 Id. 33 (1873); *Quincy, &c. R. R. Co. v. Morris*, 84 Id. 410 (1877); *Chicago, &c. R. R. Co. v. Aurora*, 99 Id. 205 (1881); *Olcott v. Supervisors*, 16 Wall. 678 (1872). But see *Weightman v. Clark*, 103 U. S. 255 (1880).

Indiana—*City of Aurora v. West*, 9 Ind. 74 (1857); *s. c.*, 22 Id. 88; *Evansville, &c. R. R. Co. v. Evansville*, 15 Id. 395 (1860); *Board of Bartholomew Co. v. Bright*, 18 Id. 93 (1862); *Thompson v. City of Peru*, 29 Id. 305 (1868); *Muncie, &c. R. R. Co. v. Geiger*, 34 Id. 185 (1870); *John v. Cincinnati, &c. R. R. Co.*, 35 Id. 539 (1871); *Commissioners of Crawford Co. v. Louisville, &c. R. R. Co.*, 39 Id. 192 (1872); *Mt. Vernon v. Hovey*, 52 Id. 563 (1876); *Indiana, &c. R. R. Co. v. Attica*, 56 Id. 476 (1877); *Williams v. Hall*, 65 Id. 129 (1879); *Bittinger v. Bell*, 65 Id. 445 (1879); *Brokaw v. Gibson Co.*, 73 Id. 543 (1881); *Peed v. Millikan*, 79 Id. 86 (1881).

Iowa (since 1869).—See the preceding note, also *McMillen v. Boyles*, 6 Iowa, 304 (1858); *Games v. Robb*, 8 Id. 193 (1859); *Chamberlain v. Burlington*, 19 Id. 395; *McMillen v. Lee Co.*, 3 Id. 311 (1858); particularly *King v. Wilson*, 1 Dillon, 555 (1871).

Kansas—*City of Atchison v. Butcher*, 3 Kan. 104 (1865); *Leavenworth Co. v. Miller*, 7 Id. 479 (1871); *Morris v. Morris Co.*, 7 Id. 570 (1871); *State v. Nemaha Co.*, 7 Id. 542 (1871); *Barnes v. Atchison*, 2 Id. 454 (1864); *Leavenworth, &c., R. R. Co. v. Douglass Co.*, 18 Id. 169 (1877).

Kentucky—*Talbot v. Dent*, 9 B. Mon. 526 (1849); *Stack v. Maysville, &c., R. R. Co.*, 13 Id. 1 (1852); *Maddox v. Graham*, 2 Metc. 56 (1859); *Shelby Co. Court v. Cumberland, &c., R. R. Co.*, 8 Bush, 209 (1871); *Allison v. Versailles, &c., R. R. Co.*, 10 Id. 1 (1873).

Louisiana—*Police Jury v. McDonough*, 8 La. Ann. 341 (1853); *Parker v. Scroggin*, 11 Id. 629 (1856). *Cf. Wilson v. Shreveport*, 29 Id. 673 (1877); *Edey v. Shreveport*, 26 Id. 636.

Maine—*Augusta Bank v. Augusta*, 49 Me. 507 (1860); *Stevens v. Anson*, 73 Id. 489 (1882).

Massachusetts—*Supervisors v. Wisconsin, &c., R. R. Co.*, 121 Mass. 460 (1877).

Minnesota—*Davidson v. Ramsey Co.*, 18 Minn. 482 (1872); *State v. Clark*, 23 Minn. 423 (1877).

Mississippi—*Strickland v. Railroad Co.*, 27 Miss. 209; *New Orleans, &c., R. R. Co. v. McDonald*, 53 Miss. 240; *Wells v. Supervisors*, 102 U. S. 625 (1880).

Missouri—*St. Louis v. Alexander*, 23 Mo. 483 (1856); *St. Joseph, &c., R. R. Co. v. Buchanan Co.*, 39 Mo. 485 (1867); *State v. Macon Co. Court*, 41 Id. 453 (1867); *Chillicothe, &c., R. R. Co. v. Brunswick*, 44 Id. 553 (1867); *State v. Linn Co.*, 44 Id. 504 (1869); *Id. v. Sullivan Co.*, 51 Id. 522 (1873); *Osage Valley, &c., R. R. Co. v. Morgan Co.*, 53 Id. 156 (1873); *Smith v. Clark Co.*, 54 Id. 58 (1873); *State v. Greene Co.*, 54 Id. 540 (1874).

Nebraska—*Hallenbeck v. Hahn*, 2 Neb. 377 (1873); *Reineman v. Covington, &c., R. R. Co.*, 7 Id. 310 (1878); *Railroad Co. v. County of Otoe*, 16 Wall. 667 (1872).

Nevada—*Gibson v. Mason*, 5 Nev. 283 (1869); *Dixon County v. Field*, 111 U. S. 83 (1884).

New Hampshire—*Perry v. Keane*, 56 N. H. 514 (1876).

New York.—See the preceding note, also *Bank of Rome v. Rome*, 18 N. Y. 38 (1858); *Starin v. Genoa*, 23 Id. 489

tion, will not avail to validate such a contract unless it is duly passed in accordance with all the constitutional formalities,¹ and after a subscription is made, any act of the legislature restricting or abridging the taxing power so as to deprive the municipality of the power to pay the bonds is unconstitutional and void.² In California, the courts go even to the extent of holding that the legislature may compel a municipality to subscribe to the stock of a railway company, and to issue its bonds in payment thereof.³ But this extreme view is disapproved in New York,⁴ and in

(1861); *People v. Mitchell*, 35 Id. 551 (1866); s. c. 45 Barb. 208; *People v. Spencer*, 55 N. Y. 1; *Duanesburgh v. Jenkins*, 66 Id. 129 (1876); *Lyons v. Chamberlain*, 86 Id. 578; *Horton v. Thompson*, 71 Id. 513 (1878); affirmed, 101 U. S. 665.

North Carolina—*Taylor v. Newbern*, 2 Jones' Eq. 141 (1855); *Caldwell v. Burke Co.*, 4 Id. 323 (1858); *Hill v. Commissioners of Forsyth Co.*, 67 N. C. 367 (1870).

Ohio—*Cincinnati, &c., R. R. Co. v. Clinton Co.*, 1 Ohio St. 77 (1852); *Steubenville, &c., R. R. Co. v. North Township*, 1 Id. 105 (1852); *Cass v. Dillon*, 2 Id. 607 (1853); *Thompson v. Kelley*, 2 Id. 647 (1853); *State v. Union Township*, 8 Id. 394 (1858); *Commissioners of Knox Co. v. Nichols*, 14 Id. 260 (1863); *Fosdick v. Perrysburg*, 14 Id. 472 (1863); *Id. v. Goshen*, 14 Id. 569 (1863); *Walker v. Cincinnati*, 21 Id. 14 (1871); s. c. *sub nom. Cincinnati v. Walker*, 1 Cin. 121 (1871).

Pennsylvania—*Commonwealth v. McWilliams*, 11 Penn. St. 61 (1849); *Brown v. Commissioners*, 21 Penn. St. 37 (1853); *Sharpless v. Philadelphia*, 21 Id. 147 (1853); *Moers v. Reading*, 21 Id. 188 (1853); *Commonwealth v. Allegheny Co.*, 32 Id. 218 (1858); *Id. v. Pittsburgh*, 34 Id. 496 (1859); *Id. v. Id.*, 41 Id. 273 (1861); *Id. v. Perkins*, 43 Id. 410; *Pennsylvania R. R. Co. v. Philadelphia*, 47 Id. 189 (1864); *Riddle v. Philadelphia, &c., R. R. Co.*, 1 Pittsb. 158 (1872); *County v. Brinton*, 47 Pa. St. 367 (1864).

South Carolina—*Copes v. Charleston*, 10 Rich. 136.

Tennessee—*Taxpayers of Milan v. Tennessee, &c., R. R. Co.*, 11 Tenn. 329; *County of Wilson v. National Bank*, 103 U. S. 770 (1880); *Nichols v. Nashville*, 9 Humph. 252 (1848); *Louisville, &c., R. R. Co. v. County Court*, 1 Sneed. 637; *Williams v. Duck River, &c., R. R. Co.*, 9

Bax. 488 (1876); *Clay v. Hawkins*, 5 Lea, 137 (1880); *Lauderdale Co. v. Ferguson*, 7 Id. 153 (1881); *Winston v. Tennessee, &c., R. R. Co.*, 57 Tenn. 60 (1873).

Texas—*San Antonio v. Jones*, 28 Texas, 19 (1866); *Id. v. Lane*, 32 Id. 405 (1869); *Id. v. Gould*, 34 Id. 49 (1870).

Vermont—*Bennington v. Park*, 50 Vt. 178 (1877); *National Bank of St. Johnsbury v. Concord*, 50 Id. 257 (1877).

Virginia—*Goddin v. Crump*, 8 Leigh, 120 (1837). See also *Goshorn v. County*, 1 West Va. 308 (1865).

Wisconsin—*Clark v. Janesville*, 10 Wis. 136 (1860); *Bushnell v. Beloit*, 10 Id. 195 (1860); *Veeder v. Lima*, 19 Id. 280 (1865); *Fisk v. Kenosha*, 26 Id. 23 (1870); *Phillips v. Albany*, 28 Id. 340 (1871); *Rogan v. Watertown*, 30 Id. 259 (1872); *Lawson v. Milwaukee, &c., R. R. Co.*, 30 Id. 597 (1872); 36 Id. 383 (1874). *Cf. Whiting v. Sheboygan, &c., R. R. Co.*, 25 Id. 167 (1870).

The leading cases upon this point are *Goddin v. Crump*, 8 Leigh, 120 (1837) (which is said by Judge Dillon, to be the first in the long series); *Leavenworth County v. Miller*, 7 Kan. 479 (1871); *Slack v. Maysville & Lexington R. R. Co.*, 13 B. Mon. 1 (1852); *Knox Co. v. Aspinwall*, 21 How. (U. S.) 539 (1858); *Sharpless v. Mayor*, 21 Penn. St. 147 (1853).

¹ *Amoskeag National Bank v. Town of Ottawa*, 105 U. S. 866 (1881); *Turner v. Commissioners of Woodson Co.*, 27 Kan. 314.

² *Wolff v. New Orleans*, 103 U. S. 358 (1880). *Cf. Edwards v. Williamson*, 71 Ala. 145, and see *Hays v. Dawes*, 75 Mo. 250 (1881).

³ *Napa Valley R. R. Co. v. Napa County*, 30 Cal. 435.

⁴ *People v. Batchelor*, 53 N. Y. 128 (1873). *Cf. Queensbury v. Culver*, 19 Wall. (U. S.) 82 (1873).

Illinois,¹ the courts in these States taking the better ground that while it is competent for the legislature to authorize a municipal subscription in a proper case, there is no power any where to compel such a subscription or donation.

While it may be conceded that, from a constitutional standpoint as well as from that of public policy and expediency, there are grave objections to the existence or exercise of this power, which has plainly been monstrously abused,² it is clear that the courts, almost universally as has been shown, have taken and will continue to hold the most liberal views as to the legislative prerogative in this respect. Such authority inhering in the legislature is generally conceded.³ It is, moreover, no objection to the validity of the legislative act, or the municipal subscription, that the subscription is made to a railway company not yet in existence. In the County of Daviess *v. Huidekoper*,⁴ it is held that county bonds in the hands of a *bona fide* holder for value are not rendered void by the fact that at the time the vote authorizing the subscription was taken, the company to be benefited was not created according to law.⁵

The legislature has power, too, before if not indeed after a subscription of this nature is made, but before it is paid, to annul the proceeding, and authorize the municipality to withdraw its subscription, and release its right to the stock.⁶ It must not be

¹ *Cairo, &c., R. R. Co. v. Sparta*, 77 Ill. 505 (1875).

² *Dillon on Munic. Corp.*, §§ 12, 117, 157; *Cooley on Const. Lim.*, § 261 *et seq.*

³ "Although it is a doctrine that must be considered as judicially settled, still it is one which has, as we think justly, encountered a vigorous opposition, both on the grounds of expediency and of power, and the exercise of authority has, as before noticed, been so disastrous, as already in some of the States, to have left to constitutional provisions for the protection of the citizens." *Dillon on Munic. Corp.*, § 158.

⁴ 98 U. S. 98 (1878).

⁵ And again in *James v. Milwaukee*, 16 Wall. 159 (1872), it is declared that an act of the legislature authorizing the city of Milwaukee to lend its credit to a specified railway company, and "to any other railroad company duly incorporated and organized for the purpose of constructing railroads," leading in a designated direction, "and which in the

opinion of the common council are entitled to such aid from the city," authorizes the lending of credit to a railroad company thereafter duly incorporated and organized as well as to those in existence when the act was passed. See also *Concord v. Portsmouth Savings Bank*, 92 U. S. 625 (1875); *Railroad Co. v. Falconer*, 103 Id. 821 (1880); *Rubey v. Shain*, 54 Mo. 207 (1873); *People v. Franklin*, 5 Lans. (N. Y.) 129 (1871).

⁶ *Aspinwall v. Jo. Daviess Co.*, 22 How. 364 (1859). *Acc. People v. Coon*, 25 Cal. 635 (1864). But see *County of Moultrie v. Rockingham, &c., Bank*, 92 U. S. 631 (1875). In *Copes v. Charleston*, 10 Rich. Law, 491 (1857), a general power conferred upon the city of Charleston, by its charter of 1793, to pass *inter alia* "every other by-law as shall appear to the city council requisite and necessary for the security, welfare, and convenience of said city," was held by the Court of Errors to authorize the city to subscribe to the stock of railway companies either within

overlooked that municipalities never have the power, by virtue of any of these legislative enactments, to tax themselves for the benefit of enterprises or objects which are private in their nature. Municipal subscriptions can only be made to the stock of companies of an essentially public character. This is a conclusively settled and plainly salutary rule.¹ Questions involving the distinction between public and private uses are constantly arising when the validity of municipal bonds is the issue, and the courts very consistently adhere to the rule that municipal aid can lawfully be extended only to railways, or other enterprises of a distinctly public or *quasi* public character.²

§ 92. *Constitutional provisions prohibiting municipal subscriptions.*—The unchecked exercise of this power on the part of the State legislatures has entailed upon the people of the States such a burden of taxation³ that in many States are found constitutional prohibitions rendering it impossible or unlawful for municipal corporations to make subscriptions or lend their credit to any incorporated company or enterprise, not strictly and exclusively governmental in its nature and constitution.

This is the case in Pennsylvania,⁴ Ohio,⁵ Illinois,⁶ New

or without the State. This is the extreme limit of the doctrine. *Cf.* City Council v. Baptist Church, 4 Strobb. Law, 306, 308 (1850).

¹ Loan Association v. Topeka, 20 Wall. 655 (1874); Weismer v. Village of Douglass, 64 N. Y. 91 (1876); Bissell v. Kankakee, 64 Ill. 249 (1872); Brewer Brick Co. v. Brewer, 62 Me. 62 (1873); Allen v. Inhabitants of Jay, 60 Id. 124 (1872); Lowell v. Boston, 111 Mass. 463; State v. Osawkee Township, 14 Kan. 418 (1875); McConnell v. Hamm, 16 Id. 228 (1876); Union Pacific R. R. Co. v. Smith, 23 Id. 745 (1880); Clark v. Des Moines, 19 Iowa, 199 (1865); Hanson v. Vernon, 27 Id. 28 (1869); Frederick v. Augusta, 5 Ga. 561 (1848); Commercial Bank v. City of Iowa, 2 Dillon, 353 (1873); Savings Assoc. v. Topeka, 3 Id. 376 (1874); Bloodgood v. Mohawk, &c., R. R. Co., 18 Wend. 965 (1837). [Compare with this case Chapman v. Gates, 54 N. Y. 132, 144 (1873).] Osborne v. Adams Co., 109 U. S. 1 (1883); s. c. 106 U. S. 181; Ottawa v. Carey, 108 U. S. 110 (1883); Freeland v. Hastings, 10 Allen, 570; Jenkins v. Andover, 103 Mass. 94 (1869); Thompson v. Pittson, 59 Me. 545 (1871); Tyson v. School Direc-

tors, 51 Penn. St. 9 (1865); People v. Salem, 20 Mich. 452 (1870); Curtis v. Whipple, 24 Wis. 350; Cook v. Manufacturing Co., 1 Sneed. (Tenn.) 698; Cooley on Const. Lim., § 212.

² A detailed consideration of this matter is properly included in treatises on constitutional law, municipal corporations, or railways, *q. v.* It may, therefore, be dismissed briefly in such a work as this.

³ Dillon on Munic. Corp. §§ 156, 160. The sum of municipal indebtedness in this country is said greatly to exceed one thousand millions of dollars, and the amount is constantly increasing.

⁴ Amend. to Const. 1857, § 7, art. II; Pennsylvania R. R. Co. v. Philadelphia, 47 Penn. St. 189 (1864).

⁵ Const., art. VIII, § 6; Walker v. Cincinnati, 21 Ohio St. 14 (1871); Cass v. Dillon, 2 Id. 607 (1853); Fosdick v. Perrysburg, 14 Id. 472 (1863); Thompson v. Kelly, 2 Id. 647 (1853); Wyscaver v. Atkinson, 37 Id. 80 (1881).

⁶ Const. 1870; Concord v. Portsmouth Savings Bank, 92 U. S. 625 (1875); Louisville v. Savings Bank, 104 U. S. 469 (1881); Harter v. Kernochan, 103 U. S. 562 (1880); Fairfield v. County of Gal-

York,¹ Indiana,² Missouri,³ Mississippi,⁴ and possibly in other States. In general it will be found that while these constitutional provisions forbid in terms any subscription or lending of credit by any municipality in the State, or by the State itself, to any company, association, or corporation whatsoever, sometimes absolutely, and at other times only when two-thirds or a majority of the qualified electors of the municipality shall assent thereto, the courts seem to incline, whenever possible, to construe the acts in such a way as to sustain the subscription, and in this way, by latitude of construction, in many instances, violence is plainly done to the spirit and intent of the statute.⁵

Inasmuch as the constitutional or statutory provisions which prohibit municipal subscriptions are of comparatively recent date, and have generally been enacted after many exercises of the legislative power sought to be restrained, it is an important rule that unless they contain express words making them retroactive they are in general construed to be prospective only.⁶

latin, 100 U. S. 47 (1879); *Chicago, &c., R. R. Co. v. Pinckney*, 74 Ill. 277 (1874); *County of Moultrie v. Rockingham Ten Cent Savings Bank*, 92 U. S. 631 (1875).

¹ Amend. Const. Jan'y 1, 1875; *People v. Fort Edward*, 70 N. Y. 28 (1877); *Dodge v. County of Platte*, 82 Id. 218 (1880), rev'g s. c. 16 Hun, 285.

² Const. art. X, § 10; *Lafayette, &c., R. R. Co. v. Geiger*, 34 Ind. 185; *John v. Cincinnati, &c., R. R. Co.*, 35 Id. 539 (1871); *Aspinwall v. Jo. Daviess Co.* 22 How. (U. S.) 364 (1859); *Brokaw v. Board of Commissioners*, 73 Ind. 543 (1881).

³ Const. art. XI, § 14; *County of Schuyler v. Thomas*, 98 U. S. 169 (1878); *Smith v. County of Clark*, 54 Mo. 58 (1873); *County of Macon v. Shores*, 97 U. S. 272 (1877); *County of Ray v. Vansycle*, 96 Id. 675 (1877); *County of Scotland v. Thomas*, 94 Id. 682 (1876).

⁴ Const. art. XII, § 14; *Supervisors v. Galbraith*, 99 U. S. 214 (1878); *Hayes v. Holly Springs*, 114 Id. 120 (1885); *Grenada Co. v. Brogden*, 112 Id. 261 (1884). Cf. *State of Minnesota v. Young*, 29 Minn. 472.

⁵ *E. g. vide Walker v. Cincinnati*, 21 Ohio St. 14 (1871); s. c. 8 Am. Rep. 24, and 11 Am. Law Reg. (N. S.) 346, and the note by Judge Redfield; *City of Savannah v. Kelly*, 108 U. S. 184 (1883); *Bank of Lawrence v. Barber*, 24 Kan. 534 (1880).

⁶ *County of Moultrie v. Rockingham Ten Cent Savings Bank*, 92 U. S. 631 (1875); *Grenada Co. v. Brogden*, 112 Id. 261 (1884); *Fairfield v. County of Galatin*, 100 Id. 47 (1879); *County of Randolph v. Post*, 93 U. S. 502 (1876); *County of Henry v. Nicolay*, 95 Id. 619 (1877); *County of Cass v. Gillett*, 100 Id. 585 (1879); *County of Calloway v. Foster*, 93 Id. 567 (1876); *Louisiana v. Taylor*, 105 Id. 454 (1881); *Jarrott v. Moberly*, 103 Id. 580 (1880); *Durkee v. Board of Liquidation*, 103 Id. 646 (1880); *Howard County v. Paddock*, 110 Id. 384 (1884); *Dallas County v. McKenzie*, 110 Id. 686 (1884), and the cases, generally, cited above.

In *Louisville v. Savings Bank*, 104 U. S. 469 (1881), it was held that the court would even take cognizance of the fractions of a day in order to do justice in such a case, and that, accordingly, the prohibitory section of the Constitution of Illinois, which went into effect July 2, 1870, would not invalidate bonds issued pursuant to a vote of the electors of the municipality, held on the morning of that day, for the purpose of determining whether a previous donation should be paid by the issue of bonds or by a special tax, the vote resulting in the determination to issue bonds.

To the same effect as to fractions of a day, see *Schall v. Bowman*, 62 Ill. 321

Neither are these constitutional prohibitions, in general, held to repeal prior statutes by which municipalities have been authorized to make subscriptions or donations to railway or other companies.¹ Accordingly, where a statute authorized a municipality to subscribe, and subsequently a constitutional provision was enacted rendering the assent of two-thirds of the voters of the town or county necessary to the validity of such a subscription, that provision was not construed as altering or impairing the effect or force of the earlier statute.²

A constitutional provision that forbids municipal subscriptions will be held to forbid equally a donation by a municipality, even in a proviso wherein a donation is not provided for in terms.³ But on the other hand it is held that a provision restricting the power of a State to make subscriptions in aid of railroads cannot be construed so as to prohibit the municipal subdivisions of the State from subscribing.⁴ And a restriction as to the power of a county will not be held applicable to a city,⁵ but school districts have no

(1872); *Richards v. Donagho*, 66 Id. 73 (1872); *Wright v. Bishop*, 88 Id. 302 (1878); *Grosvenor v. Magill*, 37 Id. 239 (1866); *Arnold v. United States*, 9 Cranch, 104 (1815); In the Matter of Joseph Richardson, 2 Story, 571 (1843); *Lapeyre v. United States*, 17 Wall. 191 (1872); *United States v. Norton*, 97 U. S. 164 (1877); *Burgess v. Salmon*, 97 Id. 381 (1878); *Kennedy v. Palmer*, 6 Gray, 316 (1876); *People v. Clark*, 1 Cal. 406 (1851); *Roe d. Maugham v. Hersey*, 3 Wils. 274 (1771); *Combe v. Pitt*, 3 Burr. 1423, 1434 (1763), by Lord Mansfield.

¹ *Cass v. Dillon*, 2 Ohio St. 607 (1853); *Louisiana v. Taylor*, 105 U. S. 454 (1881). Cf. *Oubre v. Donaldsonville*, 33 La. Ann. 366.

² *County of Henry v. Nicolay*, 95 U. S. 619 (1875). The passage of a general law is usually held not to affect a prior law special in its character. *State v. Green Co.* 54 Mo. 540 (1874); *East St. Louis v. Maxwell*, 99 Ill. 439 (1881). But see *Jeffries v. Lawrence*, 42 Iowa, 498 (1876); *Falconer v. Buffalo, &c.*, R. R. Co. 69 N. Y. 491 (1877); *List v. Wheeling*, 7 West Va. 501 (1874). Cf. *Hayes v. Holly Springs*, 114 U. S. 120 (1885); *State v. Dallas Co.*, 72 Mo. 329.

³ *Fairfield v. Gallatin Co.*, 100 U. S. 47 (1879); *Chicago, &c., R. R. Co. v. Pinckney*, 74 Ill. 277 (1874); *Lippincott v. Pana*, 92 Id. 24 (1879); *Middleport v.*

Ætna Ins. Co., 82 Id. 562 (1876). Cf. *County of Moultrie v. Fairfield*, 105 U. S. 370 (1881).

⁴ *Pattison v. Supervisors*, 13 Cal. 175 (1859); *New Orleans v. Graihle*, 9 La. Ann. 561 (1854); *Slack v. Maysville, &c.*, R. R. Co., 13 B. Mon. 1 (1852); *Leavenworth Co. v. Miller*, 7 Kan. 479 (1871); *Prettyman v. Supervisors*, 19 Ill. 406 (1858). Cf. *Bay City v. State Treasurer*, 23 Mich. 499 (1871); *Pitzman v. Freeburgh*, 92 Ill. 111 (1879).

⁵ *Thompson v. City of Peru*, 29 Ind. 305 (1868). "Whether special authority to a municipality to borrow money to pay for stock subscribed to a railway company will impliedly repeal, pro tanto, existing charter limitations upon the rate of taxation, is a question depending upon construction, and in relation to which the courts have differed. But the strong inclination of the national Supreme Court seems to be in favor of that construction which restricts such limitations to the exercise of the power of taxation in the ordinary course of municipal action." *Dillon on Munic. Corp.* § 162, citing *Butz v. Muscatine*, 8 Wall. 575 (1869). *Contra*, *Clark v. Davenport*, 14 Iowa, 494 (1863); *Learned v. Burlington*, 2 Am. Law Reg. (N. S.) 394, and note; *Leavenworth v. Norton*, 1 Kan. 432 (1863); *Burnes v. Atchinson*, 2 Id. 254 (1864). And see *Commonwealth v. Pittsburgh*, 34 Penn.

power by their trustees to subscribe to the stock of a railway, and bonds issued to pay such a subscription are void.¹

§ 93. *Power to subscribe, how to be exercised.*—The power to make municipal subscriptions being, as we have seen, statutory, it follows that in order to a valid exercise of the power, the conditions and formalities imposed by the statute must be substantially performed. There must be an essential compliance, both with the letter and the spirit of the enabling act, otherwise the subscription or security will be void.² It must appear, for example, that any constitutional or statutory requirements as to the assent to the subscription by the qualified voters of the municipality at an election, have been regularly complied with.³ The meeting must be duly called and by the proper officer;⁴ the notice of the meeting must be duly posted for the full time provided in the act.⁵ If, however, a municipal corporation should,

St. 496 (1859); *Amey v. Allegheny City*, 24 How. (U. S.) 364; *Fosdick v. Perrysburg*, 14 Ohio St. 472 (1863); *Cumberland v. Magruder*, 34 Md. 381 (1871). See *Assessors v. Commissioners*, 3 Brews. (Pa.) 333 (1869); *State v. Guttenburg*, 38 N. J. Law, 419.

¹ *Weightman v. Clark*, 103 U. S. 251 (1880). Cf. *Northern Bank v. Porter Township*, 110 Id. 608 (1884).

² *McClure v. Township of Oxford*, 94 U. S. 429 (1876); *Anderson Co. Commissioners v. Beal*, 113 Id. 227 (1885); *Carroll Co. v. Smith*, 111 Id. 556 (1884); *Hoff v. Jasper Co.*, 110 Id. 53 (1884); *Bissell v. Spring Valley Township*, 110 Id. 162 (1884); *Howard Co. v. Boonesville, &c., Bank*, 108 Id. 314 (1883); *Hawley v. Fairbanks*, 108 Id. 543 (1883); *Horton v. Town of Thompson*, 71 N. Y. 513 (1878). The U. S. Supreme Court declined, however, to follow this case in *Thompson v. Perrine*, 103 U. S. 806 (1880). *Menasha v. Hazard*, 102 U. S. 81 (1880) *Buchanan v. Litchfield*, 102 Id. 278 (1880); *Bates Co. v. Winters*, 97 Id. 83 (1877); *Hamlin v. Meadville*, 6 Neb. 227 (1877); *Cairo, &c., R. R. Co. v. Sparta*, 77 Ill. 505 (1875); *George v. Oxford*, 16 Kan. 72 (1876); *People v. Smith*, 45 N. Y. 772 (1871); *Merritt v. Portchester*, 71 Id. 309 (1877).

³ *Mustard v. Hopper*, 69 Ind. 324; *People v. Dutcher*, 50 Ill. 144 (1870); *People v. Logan County*, 63 Id. 374 (1872); *Pana v. Lippincott*, 2 Bradw. (Ill.) 466 (1877). The rule in New York upon this

point is, perhaps, especially rigorous. *People v. Smith*, 45 N. Y. 772 (1871); *People v. Hurlburt*, 46 Id. 110 (1871); *People v. Suffern*, 68 Id. 321 (1877); *Merritt v. Portchester*, 71 Id. 309 (1877); *Culver v. Fort Edward*, 8 Hun, 340 (1876); *Wilson v. Caneadea*, 15 Id. 218 (1878); *Angel v. Hume*, 17 Id. 374 (1879); *People v. Hutton*, 18 Id. 116 (1879); *People v. Barrett*, 18 Id. 206 (1879); *Wheatland v. Taylor*, 29 Id. 70 (1883).

⁴ *Town of Windsor v. Hallett*, 97 Ill. 204 (1880); *County of Richland v. People*, 3 Bradw. (Ill.) 210 (1878); *Jacksonville, &c., R. R. Co. v. Virden*, 104 Ill. 339 (1882); *Bowling Green, &c., R. R. Co. v. Warren Co.*, 10 Bush (Ky.), 711 (1874). But see *Sauerhering v. Iron Ridge, &c., R. R. Co.*, 25 Wis. 447 (1870); *Commissioners v. Baltimore, &c., R. R. Co.*, 37 Ohio St. 205 (1881).

⁵ *Harding v. Rockford, &c., R. R. Co.*, 65 Ill. 90 (1872); *Packard v. Jefferson Co.*, 2 Col. 338 (1874). Cf. *Supervisors v. Galbraith*, 99 U. S. 214 (1878). To the same effect, *Williams v. Roberts*, 88 Ill. 11 (1878); *People v. Oldtown*, 88 Id. 202 (1878). See also *Wells v. Pontiac Co.*, 102 U. S. 625 (1880); *Lincoln v. Cambria Iron Co.*, 103 Id. 412 (1880).

But where the notice was required by the statute to be "posted by the town clerk or supervisors," it was held that this did not require a posting by these officers in person, but that it was sufficient if they procured others to post the notices. Law-

before its own incorporation, assume to hold an election and vote a subscription for stock in a railway company, the vote would be a nullity, and a subscription made pursuant to such a vote could not be ratified by the corporate officers subsequently.¹ But not every failure to observe all the formalities prescribed by the enabling act is sufficient to invalidate a subscription. When it is a matter more of form than of substance that is overlooked or omitted, such an informality is not in general ground for declaring the subscription or the security void.²

It will very frequently be found, in cases that arise as to the validity of municipal subscriptions, or municipal bonds, that the subscription, or the security, is validated when the defense is the failure on the part of the municipality to comply with the requirements of the enabling act, upon the principle of estoppel, the municipality not being heard, after the lapse of time, to allege its own failure to act strictly in conformity to the statute as a defense to an action on its bonds.³

§ 94. *Submission to popular vote.*—While the legislature may usually, in the absence of a constitutional inhibition, authorize a municipality to make a subscription to the stock of a railway or

son v. Milwaukee &c., R. R. Co., 30 Wis. 597 (1872); Phillips v. Albany, 28 Id. 340 (1871); Jones v. Hurlburt, 13 N. W. Rep. 5 (1882).

¹ Clark v. Janesville, 13 Wis. 414 (1861); s. o. 10 Id. 136; Rochester v. Alfred, 13 Id. 432 (1861); Berliner v. Waterloo, 14 Id. 378 (1861); Winchester, &c., Co. v. Clark, 3 Metc. (Ky.) 140 (1860); Lewis v. Clarendon, 5 Dillon, 329 (1878).

² New Haven, &c., R. R. Co. v. Chatham, 42 Conn. 455 (1875); County of Jasper v. Ballou, 103 U. S. 745 (1880); Draper v. Springport, 104 Id. 501 (1881); Pana v. Bowler, 107 Id. 529 (1882); Lipincott v. Pana, 92 Ill. 24 (1879); Commissioners of Johnson Co. v. Thayer, 94 U. S. 631 (1876); Belfast, &c., R. R. Co. v. Brooks, 60 Me. 568 (1872); Elmendorf v. New York, 25 Wend. 693 (1841). Cf. Thomas v. City of Richmond, 12 Wall. 349 (1870); Oneida Bank v. Ontario Bank, 21 N. Y. 490 (1860); People v. Town of Santa Anna, 67 Ill. 57 (1873); People v. Town of Laenna, 67 Id. 65 (1873); Walnut v. Wade, 103 U. S. 683 (1880); Ganse v. Clarksville, 5 Dillon, 165 (1879); s. c. 1 McCreary, 78 (1880); Johnson v.

Stark, 24 Ill. 75 (1860); Clarke v. Hancock Co., 27 Id. 205 (1862); Supervisors v. Schenck, 5 Wall. 772 (1866); Singer Manfg. Co. v. Elizabeth, 42 N. J. Law, 249; Burr v. Chariton Co., 2 McCrary, 603 (1880); Henderson v. Jackson Co., 2 Id. 615 (1880).

³ Block v. Commissioners of Bourbon Co., 99 U. S. 686 (1878); Munson v. Lyons, 12 Blatchf. 539 (1875); First National Bk., &c. v. Walcott, 19 Id. 370 (1881); Harter v. Kernochan, 103 U. S. 562 (1880); Tipton Co. v. Rogers' Locomotive Works, 103 Id. 523 (1880); Menasha v. Hazard, 102 Id. 81 (1880); Amey v. Allegheny, 24 How. (U. S.) 364; Whiting v. Potter, 2 Fed. Rep. 517; Striker v. Kelly, 7 Hill (N. Y.), 9 (1844); Lamb v. Burlington, &c., R. R. Co., 39 Iowa, 333; Leavenworth, &c., R. R. Co. v. Douglas Co., 18 Kan. 169 (1877); Lyons v. Munson, 99 U. S. 684 (1878); Pendleton Co. v. Amy, 13 Wall. 297 (1877). Cf. Cagwin v. Hancock, 84 N. Y. 532 (1881); rev'g s. o. 22 Hun, 291; Orleans v. Platt, 99 U. S. 676 (1878); Wetumpka v. Wetumpka Wharf Co., 63 Ala. 611 (1879); Hackett v. Ottawa, 99 U. S. 86 (1878).

other corporation, without submitting the question to a vote of the people,¹ it has clearly the power to direct that the question shall be so submitted without rendering the act obnoxious to the objection that it amounts to a delegation of legislative powers.² It is sometimes provided that a subscription can be made only upon the petition of a certain proportion of the legal voters,³ in which case it seems that there must, in order to the validity of the petition, be a strict conformity to, and substantial compliance with, the spirit as well as the letter of the act.⁴ When the enabling act provides for municipal aid to railways and other *quasi* public enterprises upon the assent of a majority or two-thirds of the legal voters of the town or county, this is construed universally to mean that the measure is to be approved by a majority or a two-thirds vote as the case may be; that is to say, by a majority or

¹ *Thompson v. Lee County*, 3 Wall. 327 (1865); *County of Ralls v. Douglass*, 105 U. S. 728 (1881); *State v. Macon County Court*, 41 Mo. 453 (1867); *State v. County Court of Sullivan County*, 51 Id. 522 (1873). *Cf. State v. Dallas County*, 72 Id. 329 (1880); *McCallie v. Chattanooga*, 3 Head (Tenn.), 317 (1859); *Chicago, &c., R. R. Co. v. Aurora*, 99 Ill. 205 (1881); *Otoe County v. Baldwin*, 111 U. S. 1 (1883).

² *Starin v. Town of Genoa*, 23 N. Y. 439 (1861); *Gould v. Town of Sterling*, 23 Id. 456 (1861); *Bank of Rome v. Village of Rome*, 18 Id. 88 (1858); *s. o.* 19 Id. 20 (1859); *People v. Batchellor*, 53 Id. 128, 138 (1873); *Town of Duaneburgh v. Jenkins*, 57 Id. 177, 192 (1874); *Hobart v. Supervisors*, 17 Cal. 23 (1860); *Slack v. Maysville, &c., R. R. Co.*, 13 B. Mon. 1 (1852); *Winter v. City Council of Montgomery*, 65 Ala. 403 (1880). In *Harrington v. Plainview*, 27 Minn. 224 (1880), it is held that where a submission to the people is provided for, it must be to the legal voters of the municipality, and cannot lawfully be confined to resident tax-payers, whether legal voters or not. *Cf. Babcock v. Helena*, 34 Ark. 499 (1879); *Walnut v. Wade*, 103 U. S. 683 (1880). Again, where a popular vote, taken in accordance with a statute, authorized a subscription to a designated railway, and the bonds were issued to another railway, these facts appearing on the face of the bond, the invalidity of the transaction is held to appear on the face of it. *County of Bates v. Winters*, 97 U.

S. 83 (1877). *Cf. Chicot Co. v. Lewis*, 103 Id. 164 (1880); *Schaeffer v. Bonham*, 95 Ill. 368 (1880). But where a town is authorized to subscribe not exceeding a certain sum to a designated railroad, several subscriptions made at different times and authorized by as many elections, the aggregate not exceeding the amount named in the act, are valid. *Empire v. Darlington*, 101 U. S. 87 (1879). See also *Hunt v. Hamilton*, 25 Kan. 76 (1881); *Society for Savings v. City of New London*, 29 Conn. 174 (1860); *United States v. Knox County*, 2 McCrary, 625. *Cf. First Nat. Bank v. Concord*, 50 Vt. 257.

³ *E.g.* in New York. *People v. Hulbert*, 59 Barb. 446; *People v. Peck*, 62 Id. 545; *People v. Oliver*, 1 Thomp. & C. 570 (1873); *People v. Hugbitt*, 5 Lans. 89 (1871); *People v. Franklin*, 5 Id. 129 (1871); *People v. Smith*, 45 N. Y. 772 (1871); *Wellsborough v. New York, &c., R. R. Co.*, 76 Id. 182 (1879). *Cf. St. Joseph Township v. Rogers*, 16 Wall. 644 (1872); *Syracuse Savings Bank v. Seneca Falls*, 21 Hun (N. Y.), 304 (1880); *Chouteau v. Allen*, 70 Mo. 290 (1879); *Faris v. Reynolds*, 70 Ind. 360 (1880).

⁴ *Craig v. Andes*, 93 N. Y. 405; *People v. Smith*, 45 N. Y. 772 (1871), and the cases generally cited in the preceding note. See also *People v. Van Valkenburg*, 63 Barb. 105 (1872); *Evansville, &c., R. R. Co. v. Evansville*, 15 Ind. 395 (1860); *Chicago, &c., R. R. Co. v. Malloy*, 101 Ill. 583. For the manner in Indiana of contesting an election, see *Goddard v. Stockman*, 74 Ind. 400 (1881).

two-thirds of the voters who vote at the election called for the purpose, and not two-thirds or a majority of all the qualified electors in the territory. Those who fail to vote against the measure will be assumed to favor it.¹

§ 95. *What officer or agent of the municipality may make the contract of subscription.*—In the absence of any express provision in the enabling act it is plain that the proper persons to execute the contract of subscription for a municipal corporation are those whose duty it is to execute other contracts for and in the name of the municipality. A subscription is a contract, to be executed in general in the ordinary way in which any other contract may properly be made. But the act authorizing the subscription frequently provides by whom and in what manner the contract shall be executed. When this is the case the provisions of the statute are to be strictly complied with.² If the officers or

¹ County of Cass v. Johnson, 95 U. S. 360 (1877); County of Cass v. Jordan, 95 Id. 373 (1877); St. Joseph Township v. Rogers, 16 Wall. 644 (1872); Milner v. Pensacola, 2 Woods, 632 (1875); Reiger v. Beaufort, 70 N. C. 319 (1874); Hawkins v. Carroll Co., 50 Miss. 735 (1874); Louisville, &c., R. R. Co. v. Tennessee, 8 Heisk. 663 (1875); Woodson v. Brassfield, 67 Mo. 331 (1878); Webb v. La Fayette Co., 67 Id. 353 (1878); People v. Chapman, 66 Ill. 137 (1872); People v. Hoop, 67 Id. 62 (1873); Melvin v. Lisenby, 72 Id. 63 (1874); Harrington v. Plainfield, 27 Minn. 224 (1880). See also Cagwin v. Hancock, 84 N. Y. 532 (1881); Springport v. Teutonia Savings Bank, 84 Id. 403 (1881). And for a contrary rule well argued out, see Harshman v. Bates Co., 92 U. S. 596 (1875) [overruled, however, in County of Cass v. Johnson, 95 U. S. 360 (1877)], and the dissenting opinions of Miller and Bradley, JJ., in County of Cass v. Johnson, 95 U. S. 360, 370 (1877). As to the right of a voter or signer to revoke his consent once granted, see People v. Wagner, 1 Thomp. & C. 221 (1873); People v. Deyoe, 1 Id. 142; People v. Hatch, 1 Id. 113 (1873). Cf. First Nat. Bank v. Dorset, 16 Blatchf. 62 (1879); Noble v. Vincennes, 42 Ind. 125 (1873), and see Monadnock R. R. Co. v. Peterboro, 49 N. H. 281 (1870); Hannibal v. Fountleroy, 105 U. S. 408 (1881). If a legislature have power to authorize a subscription to the stock of a railway company by a township, and to

provide, as a condition precedent to such a subscription, that a majority of the legal voters of such township signify their assent thereto, it has the power to legalize an election held for that purpose before the passage of the act of authorization, and to validate a subscription so made. While the courts of the United States accept and apply the construction of a State constitution, or of a local statute upon which the rights of parties depend, which has been fixed by the course of decisions of the State courts, it is the settled doctrine of the Supreme Court of the United States that rights accruing under one construction will not be lost or forfeited merely by a change of opinion in the State court; and when such rights have accrued before the State court has announced its construction, the Federal courts, although leaning to an agreement with the State courts, will determine the matter upon their own independent judgment. Anderson v. Township of Santa Anna, Sup. Ct. U. S. Feb'y 8, 1886. Cf. State v. Holladay, 72 Mo. 499; Smith v. City of Fon du Lac, 8 Fed. Rep. 289; McCall v. Town of Hancock, 10 Id. 8; Carroll Co. v. Smith, 111 U. S. 556 (1884); Green Co. v. Conness, 109 U. S. 104 (1883).

² Walnut v. Wade, 103 U. S. 683 (1880); People v. Smith, 45 N. Y. 772 (1871); Town of Douglass v. Niantic Savings Bank, 97 Ill. 228 (1881). So, for example, where the act provides for the appointment of a board of commissioners to

agents of a municipality have a discretion with reference to the subscription, to make it or not as it may seem to them best under the circumstances, their exercise of that discretion is final, and cannot be reviewed or questioned.¹ But a corporation cannot be bound by the act of an agent, if it appears that the other contracting party is in any way affected with knowledge that the contract to bind the company should be signed by certain officers or agents, the contract sought to be enforced not having been so executed, which is to say, that a contract signed by an agent not authorized to sign, cannot bind a corporation when the other party knew or ought to have known that some other agent was the proper person to enter into the contract on behalf of the corporation, and that the agent assuming to act was in reality unauthorized.²

§ 96. *Formal requisites of a municipal subscription.*—Nugent v. The Supervisors,³ is the leading case. Therein it is held, that in order to constitute a valid municipal subscription to the stock of a railway company, it is not necessary that there be an actual act of chirographical subscribing; that a resolution by a duly authorized board of agents, declaring a subscription made, is, upon the acceptance of the subscription in that shape by the railway company, and a notice to the municipality of the acceptance, a good and binding subscription, although there was no subscription made in the books of the company, and that the delivery by the proper officers of the municipality to the rail-

make the subscription, they only are competent to make it; they are for this purpose the agents of the municipality for which they act; they may insert conditions into the contract which, unless repudiated by the corporation, are valid, and will bind all parties concerned; their powers are to be exercised jointly, and therein all must act, a majority not being sufficient by their act to bind the municipality; their acts, when once fully performed, are final and binding, and cannot be recalled or revoked. Danville v. Montpelier, &c., R. R. Co., 43 Vt. 144 (1870); cf. First Nat. Bank v. Arlington, 16 Blatchf. 57 (1879); People v. Hitchcock, 2 N. Y. Super. Ct. 134 (1873); State v. Hancock Co., 11 Ohio St. 183 (1860); s. o. 12 Id. 596; Jackson Co. v. Brush, 77 Ill. 59 (1875); Walnut v. Wade, 103 U. S. 683 (1880); People v. New York, &c., R. R. Co., 84 N. Y. 565 (1881); Kankakee v. Aetna Life Ins. Co., 106 U. S. 668 (1882);

Bissell v. Township of Spring Valley, 110 U. S. 162 (1884); *In re Bradner*, 87 N. Y. 171 (1881).

¹ Mercer Co. v. Pittsburgh, &c., R. R. Co., 27 Penn. St. 389 (1856). Cf. Falconer v. Buffalo, &c., R. R. Co., 69 N. Y. 491 (1877); First Nat. Bank v. Concord, 50 Vt. 257.

² Head v. Providence Ins. Co., 2 Cranch, 127 (1804); Holbrook v. Fanquier, &c., Co., 3 Cranch C. C. 425 (1829); Henning v. United States Ins. Co., 47 Mo. 425 (1871); Badger v. Am., &c., Ins. Co., 103 Mass. 244 (1869); Dana v. Bank of St. Paul, 4 Minn. 385 (1860); Barnes v. Ontario Bank, 19 N. Y. 152 (1859); Bulkley v. Derby Fishing Co., 2 Conn. 252 (1817); Salem Bank v. Gloucester Bank, 17 Mass. 1 (1820); Walton's Case, 26 L. J. Chan. 545 (1857). This is, of course, a general rule of law, and one applicable to all contracts executed by agents of corporations.

³ 19 Wall. 241 (1873).

way company of the municipal bonds in exchange for the stock—the levying of a tax to pay the interest on the bonds—and voting as a share owner, estops the corporation from denying the subscription.¹

But the vote of the tax-payers or inhabitants, as the case may be, is not a subscription, nor does it amount to a subscription, nor does it in general vest in the company, for whose proposed benefit the vote was taken, a right to have a subscription made.² There will generally vest in the corporate officer, expressly or by implication, some discretion, even after the election, as to the subscription, or it will devolve upon them to do certain acts or insist upon certain conditions, and hence until such acts are performed; or the conditions made, there is, by virtue of the mere vote, no valid subscription.³

§ 97. *Municipal conditions may be conditional.*—A municipal corporation may, as of course, in the absence of statutory prohibition, annex to its subscription any condition that an individual subscriber might lawfully prescribe, and may, in consequence, make the payment of the subscription depend upon the performance thereof.⁴ So also is a municipal corporation entitled to the benefit of any implied conditions, arising from the act of incorporation, or by intendment of law, to which an individual subscriber would be entitled.⁵

In the case of the *Madison County Court v. Richmond, &c.*,

¹ This is the settled rule of the Supreme Court of the United States. *County of Moultrie v. Rockingham Ten Cent Savings Bank*, 92 U. S. 631 (1875); *County of Cass v. Gillett*, 100 Id. 585 (1879). *Cf.* *State v. Jennings*, 4 Wis. 549.

² *Cumberland, &c., R. R. Co. v. Barren Co.*, 10 Bush (Ky.), 604 (1874); *Bates County v. Winters*, 97 U. S. 83 (1877); *Wadsworth v. St. Croix Co.*, 4 Fed. Rep. 378 (1880). *Cf.* *Allen v. Louisiana*, 103 U. S. 80 (1880).

³ *People v. Pueblo Co.*, 2 Cal. 360 (1874), and the cases in the preceding note. *Winter v. City Council of Montgomery*, 65 Ala. 403 (1880); *Syracuse Savings Bank v. Town of Seneca Falls*, 86 N. Y. 317 (1881). *Cf.* *Bank of Statesville v. Town of Statesville*, 84 N. C. 169 (1881). The bonds if signed on

Sunday will be invalid, although the signature is by the proper officer. *DeForth v. Wisconsin, &c., R. R. Co.*, 52 Wis. 320 (1881).

⁴ *Brokaw v. Gibson Co.*, 73 Ind. 543 (1881); *Portland, &c., R. R. Co. v. Inhabitants of Hartford*, 58 Me. 23 (1870); *Chicago, &c., R. R. Co. v. Aurora*, 99 Ill. 205; *Noesen v. Port Washington*, 37 Wis. 168 (1875); *Perkins v. Port Washington*, 37 Id. 177 (1875); *Town of Platteville v. Galena, &c., R. R. Co.*, 43 Id. 493 (1878); *Foote v. Mount Pleasant*, 1 McCrary, 101 (1878); *Atchison, &c., R. R. Co. v. Phillips Co.*, 25 Kan. 261 (1881). *Cf.* *Memphis, &c., R. R. Co. v. Thompson*, 24 Kan. 170 (1880); *Red Rock v. Henry*, 106 U. S. 576 (1882); *Shurtleff v. Wisconsin*, 74 Me. 130 (1882).

⁵ *Lamb v. Anderson*, 54 Iowa, 100 (1880).

R. R. Co.,¹ it is held that, while a county may make such conditions as may seem proper to it before submitting the question of a subscription to a popular vote, the county court cannot, after the vote is taken, require other conditions, or alter those already imposed, or by a second election change the terms of the contract of subscription as originally made and entered into.²

Where a condition precedent has not been fulfilled, the subscription is not enforceable, and bonds issued in payment will be invalid even in the hands of *bona fide* holders; as for example, where the location of a railway in a certain place is the condition, and the location is not made as required by the condition.³ But if it be a condition subsequent, as where a town subscribed for stock in a railway company, upon condition that the road should "be built through the town on the line as run by the engineer, with a suitable depot for the convenience of the public," a failure to perform is not a defense to an action to collect assessments.⁴ In New York it is held that where a town imposes as a condition precedent to its subscription that the road be located and constructed through the town, the commissioners have no power to accept any agreement from the company or any substitute in lieu of full compliance.⁵

§ 98. *A municipal subscription may be paid in bonds instead of money.*—Generally it may be said that, where a municipal corporation is authorized to subscribe to the stock of a railway or other corporation, or to lend its credit thereto, and to issue bonds to that end, it may, in the exercise of its proper discretion, instead of selling the bonds and applying the proceeds to the payment of the subscription, deliver the bonds themselves to the railway company in exchange for an equivalent amount of the stock.⁶ The

¹ 80 Ky. 16 (1882).

² *Acc. Carroll Co. v. Smith*, 111 U. S. 556 (1884).

³ *Mellen v. Town of Lansing*, 19 Blatchf. 512 (1871); *Chicago, &c., R. R. Co. v. Marseilles*, 84 Ill. 145 (1876); *Bucksport, &c., R. R. Co. v. Brewer*, 67 Me. 295 (1877).

⁴ *Belfast, &c., R. R. Co. v. Brooks*, 60 Me. 568 (1872). *Cf. Chicago, &c., R. R. Co. v. Schewe*, 45 Iowa, 79 (1876). See also *People v. Holden*, 82 Ill. 93 (1876); *Hodgman v. St. Paul, &c., R. R. Co.*, 23 Minn. 153 (1876); *State v. Town of*

Clark, 23 Id. 422 (1877); *State v. Lime*, 23 Id. 521 (1877).

⁵ *Falconer v. Buffalo, &c., R. R. Co.*, 69 N. Y. 491 (1877). As to the right to revoke a consent by popular vote, see *Town of Springport v. Teutonia Savings Bank*, 84 N. Y. 403 (1881).

⁶ This is the learning in the case of *Meyer v. the City of Muscatine*, 1 Wall. 384, 392 (1863), and except in New York, *Starin v. Genoa*, 23 N. Y. 439 (1861); *Bank of Rome v. Village of Rome*, 19 Id. 20 (1859), it is a generally accepted rule of law. *Acc. Evansville, &c., R. R. Co. v.*

objection to this doctrine, as urged by the Court of Appeals of New York, proceeds upon the ground that a town might prudently and properly undertake to negotiate its own bonds and use the proceeds to pay for stock in a railway company, while it might be very improvident and unjust to allow the railroad company to take the bonds and negotiate them for very much less than their par value; which is to say, that public policy dictates that municipal subscriptions should be made to realize the full amount to the company, in order that the public convenience contemplated by the building of the railway may be most economically and completely subserved.¹ The force of this objection may be conceded, but it is, perhaps, rather an apparent than a real difficulty. The statute authorizing the issue of bonds usually provides that they are not to be negotiated for less than par, and, in the absence of such a statutory provision, the courts hold, on general common-law grounds, that such bonds cannot lawfully be sold for less than par;² and if they are sold, in violation of the inhibition of the statute, below par, the corporation may in equity compel the holder to accept in satisfaction the sum paid by the original purchaser, with lawful interest.³

§ 99. *A municipal corporation as a stockholder.*—When a municipal corporation subscribes to the stock of a railway company, it thereby incurs in all respects the same liability that attaches to any other shareholder in the company. It becomes, in other words, a stockholder in just the same sense as any individual subscriber, entitled to the same rights, privileges, and emoluments, and subject to the same burdens of duty and liability as the other holders of the stock.⁴

City of Evansville, 15 Ind. 395 (1860); Curtis v. County of Butler, 24 How. (U. S.) 435; Commonwealth v. Pittsburgh, 41 Penn. St. 278; Town of Concord v. Portsmouth Savings Bank, 92 U. S. 625 (1871); Town of Montclair v. Ramsdell, 107 U. S. 147 (1882).

¹ See *Starin v. Genoa*, *supra*, at p. 454.

² *Neuse River Navigation Co. v. Commissioners of Newbern*, 7 Jones (N. C.), 275; Dan. Neg. Instr. (3d ed.), § 1533.

³ *County of Armstrong v. Brinton*, 47 Penn. St. 357 (1864).

⁴ *Shipley v. The City of Terre Haute*,

74 Ind. 297 (1881), is the leading case. In the opinion Woods, J., says: "By the act of May 4, 1869, the legislature made an express grant to the defendant of the power to become a stockholder in a railroad company. So far as in their nature they could be exercised or enjoyed, it is clear that the rights and privileges of an ordinary stockholder belonged to the city when it became a stockholder as alleged, and it seems to be equally clear that in conferring the power to acquire the rights and benefits the legislature must have intended to impose the attendant burdens. Indeed, the right conferred has no legal

This doctrine is not only declared in the cases cited in the notes, but it is assumed to be an unquestioned rule of law in all that long line of cases, both in the State and Federal courts, which involves the validity of municipal bonds issued in aid of railway or other corporations.

§ 100. *A municipality may enforce delivery of stock to itself in a proper case.*—Under the same circumstances and conditions, and to the same extent as any other subscriber, a municipal corporation may compel a railway or other corporation to deliver to it stock to which the subscribers in general are entitled. It is entitled, like any other subscriber, to whatever it has subscribed for and paid for. Whatever would prevent an individual subscriber from enforcing such delivery will equally prevent a municipality in a like case.¹ So it is said that a municipal corporation, or a subscriber, is in no better position than an individual subscriber in this respect.² The cases plainly make no distinction as to the right to enforce delivery of stock between classes of subscribers, and the municipal subscriber has no more and no less right in respect thereto than other subscribers.

§ 101. *Change in the State constitution, or the general statutory law, after the municipal corporation has voted to subscribe.*—Constitutional provisions, or general statutes prohibiting municipal corporations from subscribing to the stock of other corpora-

existence or definition apart from the duties and obligations expressly connected therewith."

In *Gray v. The State*, 72 Ind. 567 (1880), it is said: "We see no reason why the State, as a debtor, should be placed in any other or different situation as to its obligation to pay interest than that occupied by any private debtor or other public corporation." 1 Dan. Neg. Instr., § 436; *Murray v. Charleston*, 96 U. S. 432.

In the case last above cited, the court said, at page 445: "The truth is, States and cities, when they borrow money and contract to repay it with interest, are not acting as sovereignties. They come down to the level of ordinary individuals. Their contracts have the same meaning as that of similar contracts between private persons."

Acc. Curran v. The State, 15 How. 304;

Robinson v. Bank of Darien, 18 Ga. 65; *National Bank v. Case*, 99 U. S. 628 (1878). See also *Wood on Railways*, § 118, citing to the point that a municipal subscription makes a municipal corporation stand in the same relation to the company and the public as any other shareholder. *County of Morgan v. Allen*, 103 U. S. 498 (1880); *Sawyer v. Hoag*, 17 Wall. 610 (1873); *Sanger v. Upton*, 91 U. S. 56 (1875); *Upton v. Tribilcock*, 91 Id. 45 (1875); *Webster v. Upton*, 91 Id. 65 (1875); *Hatch v. Dana*, 101 Id. 205 (1879); *Bank of U. S. v. Planters' Bank*, 9 Wheat. 904; *Morgan County v. Thomas*, 76 Ill. 120 (1875); *State v. Holladay*, 72 Mo. 499.

¹ *Wapello Co. v. Burlington, &c. R. R. Co.*, 44 Iowa, 585 (1876).

² *Pittsburgh, &c., R. R. Co. v. Allegheny Co.*, 79 Penn. St. 210 (1875). *Cf. State v. Garoutte*, 67 Mo. 445 (1878).

tions, or from lending their credit thereto, are, as we have seen,¹ wholly prospective in their application.

What a corporation had the constitutional or statutory right to do, and what it has done in pursuance of that right or authority, cannot be affected or undone by subsequent constitutional change or amendment, or by the passage of general statutes. This is a fundamental rule of constitutional law, and a brief application of it here will suffice.² If it be held that a popular vote does not give the company proposed to be benefited a vested right to the subscription by the municipality, and that until the subscription is actually made, the contract is unexecuted, and therefore obligatory upon neither party, there is ground for holding that a constitutional prohibition, taking effect after the election, but before the subscription is made pursuant to authority conferred by the popular vote, will be sufficient to invalidate the subscription. This was the view taken by the Supreme Court of the United States in the case of *Aspinwall v. Commissioners of the County of Daviess*,³ and affirmed in some later cases.⁴ The weight of authority however is, it is believed, in favor of the rule that, after the corporation has, by a popular vote at an election lawfully held, voted to subscribe for stock, subsequent changes of the constitution or the general statutes will not affect the right of the municipality to go on and complete the contract; that is to say, to make the formal subscription, and to issue the bonds or levy the special tax to pay the calls.⁵

¹ § 92.

² Accordingly we find it held that the constitution of 1870, of the State of Illinois, which prohibits municipal subscriptions or donations, does not attempt to affect or impair the obligation of any prior contract with respect thereto, nor prohibit the issue of bonds which are necessary to give effect to subscriptions or donations which were authorized by a popular vote, cast at an election lawfully held, before the day on which the constitution went into effect.

County of Clay v. Society for Savings, 104 U. S. 579 (1881); *People v. Logan County*, 63 Ill. 374 (1872); *County of Moultrie v. Savings Bank*, 92 U. S. 631 (1875); *Louisville v. Savings Bank*, 104 Id. 469 (1881). To the same effect, with regard to the constitution of 1875, of Ne-

braska, see *State v. Lancaster Co.*, 6 Neb. 214; and as to the constitution of Missouri, of 1865, see *Louisiana v. Taylor*, 105 U. S. 454 (1881); *County of Cass v. Gillett*, 100 Id. 585 (1879); *County of Scotland v. Thomas*, 94 Id. 682 (1876); *County of Ray v. Vansycle*, 96 Id. 675; *County of Calloway v. Foster*, 93 Id. 567 (1876).

³ 22 How. 364 (1859).

⁴ *Wadsworth v. Supervisors*, 102 U. S. 534 (1880). See also *Railroad Co. v. Falconer*, 103 Id. 821 (1880).

⁵ See the cases generally cited *supra*, and *United States v. Jefferson Co.*, 5 Dillon, 310 (1878); *Maenhant v. New Orleans*, 3 Woods, 1 (1876); *Sibley v. Mobile*, 3 Id. 535 (1876); *Nicolay v. St. Clair County*, 3 Dillon, 163 (1874); *Huidekoper v. Dallas County*, 3 Id. 171 (1875). *Cf. Red Rock v. Henry*, 106 U. S. 576 (1882).

§ 102. *Division of the municipality after the subscription.*—

We find a line of cases in the reports of some of the Western States, which deal with the questions which have grown out of the subdivision of towns and counties in those States, after a donation or subscription has been made to some railway or other corporation, and before the bonds have been issued, or before they have become due and payable.

It is, of course, not competent for the legislature so to divide a municipality as to release all or any part of it from the obligation of any contract into which the whole had previously entered.¹ When a town or county is divided, or some part of it annexed to some other town or county, after the undivided municipality has voted a subscription, and it is provided in the act by which the division is accomplished, that each part shall remain liable for the previous municipal indebtedness, such provision is held to mean nothing more than that, as concerns the subscription voted, each part is liable for its proportion only of the debt according to the valuation of the property of the undivided municipality at the time the vote was taken.²

§ 103. *Consolidation of companies after the municipal aid is voted.*—When the company proposed to be benefited, unites or is consolidated with another company or companies of a similar character, after the aid of a municipality has been voted, and before the subscription has been paid, the company having before the election the right to consolidate, the bonds may lawfully be issued to or sold for the benefit of the new or consolidated company.³ When, however, the consolidation works such a fundamental change in the constitution and purpose of the original corporation that individual subscribers are thereby released, a

¹ *Sedgwick Co. v. Bailey*, 11 Kan. 631 (1873). *Cf. State v. Lake City*, 25 Minn. 504 (1879); *Marion Co. v. Harvey Co.*, 26 Kan. 181 (1881); *Henderson v. Jackson Co.*, 12 Fed. Rep. 676 (1881).

² *Hurt v. Hamilton*, 25 Kan. 76 (1881). See also *Eagle v. Beard*, 33 Ark. 497 (1878); *McBride v. Hardin Co.*, 58 Iowa, 219 (1882).

³ *New Buffalo v. Iron Company*, 105 U. S. 73 (1881); *County of Scotland v. Thomas*, 94 Id. 682 (1876); *Town of East Lincoln v. Davenport*, 94 Id. 801 (1876);

Wilson v. Salamanca, 99 Id. 499 (1878); *Empire v. Darlington*, 101 Id. 87 (1879); *Menasha v. Hazard*, 102 Id. 81 (1880); *Harter v. Kernochan*, 103 Id. 562 (1880); *County of Tipton v. Locomotive Works*, 103 Id. 523 (1880); *State v. Green Co.*, 54 Mo. 540 (1874); *Vernon v. Hovey*, 52 Ind. 563 (1876). See also *Nugent v. Supervisors*, 19 Wall. 241 (1873); *County of Henry v. Nicolay*, 95 U. S. 619 (1877); *County of Schuyler v. Thomas*, 98 Id. 169 (1877). *Cf. Harshman v. Bates County*, 92 U. S. 569 (1875).

subscription by a municipality will be invalidated,¹ but otherwise not.² It is accordingly said that municipal bonds voted and delivered to a corporation under a changed name are not by such change invalidated.³

¹ *Lynch v. Eastern, &c. R. R. Co.*, 57 Wis. 430 (1883); *Harshman v. Bates County*, *supra*, will hardly be followed. It does not accord with the current decisions. Cf. *Taylor on Corp.*, § 324.

² *Atchison, &c., R. R. Co. v. Phillips Co.*, 25 Kan. 261 (1881); *Society for Savings v. New London*, 29 Conn. 174 (1860); *Commonwealth v. Pittsburgh*, 41 Penn. St. 278 (1861); *Illinois, &c. R. R. Co. v. Barnett*, 85 Ill. 313 (1877); *Lewis v. Clarendon*, 5 Dillon, 329 (1878); *Chickaming v. Carpenter*, 106 U. S. 663 (1882).

³ *Town of Reading v. Wedder*, 66 Ill. 80 (1872). Cf. *Town of Prairie v. Lloyd*, 97 Id. 179 (1880). In the case of *Marsh v. Fulton Co.*, 10 Wall. 676 (1870), where the legislature so amended the charter of

a railway company as to divide the road into three divisions, and each division was made a new company, so that there were three distinct corporations in place of the original corporation, it was held by the Federal Supreme Court, that a subscription of stock and issue of county bonds, authorized by a popular vote to be made to the original corporation, could not legally be made to one of the three new corporations. The court may, perhaps, have regarded this as a case of novel impression. Mr. Justice Field, in delivering the unanimous judgment of the court, cited no authorities, but seemed, in an opinion of some length, to proceed to the conclusion upon general considerations of policy and convenience.

CHAPTER VII.

CALLS.

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| <p>§ 104. Definition of call.
105. Call is generally necessary.
106. When a call is unnecessary.
107. In New York, no call is required.
108. In case of corporate insolvency, no call is necessary.
109. Who has authority to make calls.
110. Calls by directors.
111. Assignment of subscriptions by corporation, before or after call.
112. Interest runs from the time the call is due.
113. Stockholder cannot question advisability of call.</p> | <p>114. Calls must be impartial and uniform.
115. Method of making calls.—No formalities necessary.
116. Time, place, amount, and person to whom payable.
117. Notice of calls.—Cases holding it not necessary.
118. — Cases holding it to be necessary.
119. Methods of serving notice of calls.
120. Demand, waiver, pleadings, &c.</p> |
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§ 104. *Definition of call.*—A “call” may be defined to be an official declaration, by the proper corporate authorities, that the whole or a specified part of the subscriptions for stocks required to be paid.¹ The term, however, is used with different meanings, and may refer to the resolution of the officials that a part or the whole of the subscription must be paid, or to the resolution and notification thereof, or the combination of facts making the parties called on liable to an action for non-payment of the money called.² An assessment is a term often used to designate the same thing as a call, but sometimes refers to payments sought to be recovered from the stockholders, above and in addition to the par value of the stock. An instalment is one of the several part payments which may be included in a single call.

¹ *Braddock v. Phil. Marlton & Medford R. R. Co.*, 45 N. J. L. 363 (1883), holding also that a direction by the directors to the President to collect the subscriptions is a call. In the case *Spangler v. Ind. & Ill. Central R. Co.*, 21 Ill. 276 (1859), a call or assessment is rather vaguely defined as “a rating or fixing of the proportion by the board of directors, which every subscriber is to pay of his subscription, when notified of it and when called in.” *Newry & Enniskillen Ry.*

Co. v. Edmunds, 2 Ex. Rep. 118 (1848), holds that a call is an application to each shareholder for a proportion of his share.

² *Queen v. Londonderry & Coleraine Ry. Co.*, 13 Q. B. 998. In *Ambergate, N. & B. & E. J. Ry. Co. v. Mitchell*, 4 Ex. Rep. 540 (1849), it is said “the word call is capable of three meanings. It may either mean the resolution, or its notification, or the time when it becomes payable. It must mean either one of these three.”

§ 105. *Call is generally necessary.*—As a general rule, a call must be made before a subscription or any part thereof becomes due and payable to the corporation. A contract of subscription, unlike other contracts to pay money, is a promise to pay only at such times, and in such part payments, as may be designated by the corporate authorities in a formal declaration known as a "call."¹ In other words, the subscription is a debt payable at a future time.² The time when it shall be paid is indefinite until fixed by a call.

§ 106. *When a call is unnecessary.*—If, however, a subscription contains a promise to pay upon a certain day, no call is necessary, but the subscriber is bound to pay, at all events, upon the day named.³ So also if by statute or the charter the subscription becomes payable at a certain specified time, a call is

¹ "No action can be maintained against a stockholder for an instalment on his subscription until the board has directed the call to be made." *Banet v. Alton & Sangamon R. R. Co.*, 13 Ill. 504 (1851); *Spangler v. Ind. & Ill. Central R. R. Co.*, 21 Ill. 276; *Braddock v. Phil., Marlton & Medford R. R. Co.*, 45 N. J. L. 363 (1883). In the case *Grasse Isle Hotel Co. v. L'Anson's Ex'rs*, 42 N. J. L. 10 (1880); *aff'd* 43 N. J. L. 442 (1881), the court said a subscription for stock "imports an agreement not to pay at once the whole sum representing the value of the shares subscribed for, but a stipulation to pay such sum when called for by the directors, in amounts duly assessed." And in *Bk of South Australia v. Abrahams, L. R.*, 6 Privy Council App. 262 (1875), the court said: "The company has no absolute right, and the shareholder is under no absolute liability, to pay. The right only arises if, and when, calls are made by the directors. . . . The due making of the call by the resolution of a board of directors is an essential condition precedent." To the same effect, see *Wilbur v. Stockholders of the Corp'n.*, 18 Bankr. Reg. 178. Where, by statute or charter, payment is to be in such manner, and proportion, and times, as the directors may order, there can be no suit to collect until after a call. *Grissell's Case*, L. R., 1 Ch. App. 528, 535 (1866); *Ala. & Fla. R. R. Co. v. Rowley*, 9 Fla. 505 (1861). Even where the stock is fraudulently issued as paid up, in payment for property, and the transaction is impeached for fraud, a call is necessary

before the subscription can be enforced. *Granite Roofing Co. v. Michael*, 54 Md. 65 (1880). Where, however, for failure to furnish the property due on a subscription, a suit for damages is brought by the corporation, no call need precede such suit. An allegation of a general demand suffices. *Cheraw & Chester R. R. Co. v. Garland*, 14 S. C. 63 (1879); *Ohio, Ind. & Ill. R. R. Co. v. Cramer*, 23 Ind. 490 (1864). A call is not applicable to stock which was subscribed for after the call was made. *Pike v. Shore Line*, 68 Me. 445 (1878).

² The subscription "is a present debt, payable at a future day." *Pittsburgh & Connellsville R. R. Co. v. Clarke*, 29 Pa. St. 146 (1857). The subscription "creates a debt, but the debt does not accrue due till a call is made." *Grissell's Case*, L. R., 1 Ch. App. 528, 535 (1866); *In re China Steamship & L. Coal Co.*, 38 L. J. (Ch.) 512 (1869), the court says: "The moment a call is made, it is a debt due in every respect," although it cannot be collected by suit until later. The bankruptcy act does not release an applicant thereunder from liability for calls made after his release in bankruptcy. *Glenn v. Howard*, 3 Atl. Rep. 895 (1886).

³ *Estell v. Knightstown & Middletown Turnpike Co.*, 41 Ind. 174 (1872); *New Albany & Salem R. R. Co. v. Pickens*, 5 Ind. 247 (1854); *Ross v. Lafayette & Indianapolis R. R. Co.*, 6 Ind. 297 (1853); *Brudlove v. Martinsville & F. R. R. Co.*, 12 Ind. 114 (1859); *Waukon & M. R. R. Co. v. Dwyer*, 49 Iowa, 121 (1878).

thereby dispensed with, and is not required.¹ A stockholder, on the other hand, is not obliged to wait for a call even when entitled to it. He may pay at any time.²

§ 107. *New York rule.*—In New York it seems that a different rule prevails. In that State there is a tendency to hold that no call is necessary before suit is brought on a subscription for stock. The subscriber's obligation to pay, and the time and manner of payment, must be sought for in the contract itself. Unless the contract provides for calls, the subscription is payable absolutely, and at once or as soon as the corporation is duly organized.³ Accordingly, in an action brought to collect a subscription, it is not necessary to allege that a call has been made, unless the terms of the subscription or the provisions of the corporate charter expressly provide for calls. These rules, however, seem not to have been directly passed upon in New York, and it is doubtful whether they can be considered as clearly established in that State.⁴

§ 108. *In case of corporate insolvency, no call is necessary.*—When a corporation becomes insolvent, and there exist subscriptions which have not been fully paid in, the directors frequently neglect or refuse to make calls for the purpose of paying the cor-

¹ *Phoenix Warehousing Co. v. Badger*, 67 N. Y. 294 (1876).

² *Marsh v. Burroughs*, 1 Woods, 463 (1871); *Poole's Case*, L. R., 9 Ch. D. 322 (1878). But if such payment is by the directors themselves, and it is immediately repaid to them for fees, the corporation being insolvent, the transaction will be set aside. *Syke's Case*, L. R., 13 Eq. Cas. 255 (1871). So also a payment in advance, on an agreement, that such payment shall be only a loan if the corporation is successful, but shall be a payment of the subscription if the corporation becomes insolvent, is held to be a loan, though insolvency occurs. *Barge's Case*, L. R., 5 Eq. Cas. 420 (1868). Frequently a subscription is paid, before a call, by applying to its payment money due the subscriber from the corporation. *Adamson's Case*, L. R., 18 Eq. Cas. 670 (1874).

³ *Lake Ontario, Auburn & N. Y. R. R. Co. v. Mason*, 16 N. Y. 451 (1859); *Phoenix Warehousing Co. v. Badger*, 67 N. Y. 294, 300 (1876). In the former case, however, calls were made and notice given by advertisement in a newspaper. In the latter

case, by the terms of the charter, all subscriptions were due at the time when suit was commenced. Hence, in both cases, the statements in reference to calls have the appearance of *dicta*. In *Mann v. Pentz*, 3 N. Y. 415 (1850), it was held that a receiver could not collect uncalled subscriptions, since "the only condition upon which he (the subscriber) could have been made liable to the corporation, was by regular calls made in pursuance of the charter." See also *Bauton v. Dry Dock, Gd. St. & S. F. Stage Co.*, 4 E. D. Smith, 420 (1855); *Seymour v. Sturgess*, 26 N. Y. 134 (1862); *Savage v. Medbury*, 19 N. Y. 32 (1859).

⁴ These rules seem to be peculiar to New York. The decisions in some of the other States, hold, however, that no notice of calls is necessary. See § 117. Practically such a rule is equivalent to requiring no call at all, since in both cases collection is made only upon orders of the directors or other officers, and in both cases the subscriber is not informed of such orders.

porate debts. In such cases a court of equity will disregard the formality of a call, and will order the unpaid subscriptions to be paid to a receiver for the benefit of the corporate creditors.¹

The courts may properly hold that it is not discretionary with the directors to say whether the company's debts shall be paid or not. And this is the rule even though the statute provide that calls shall be made by the directors.² There has been some doubt as to whether the writ of mandamus would lie to compel the directors to make the call,³ but the authorities seem to hold that

¹ "It is well settled that when stock is subscribed to be paid upon call of the company, and the company refuses or neglects to make the call, a court of equity may itself make the call, if the interests of the creditors require it." *Scoville v. Thayer*, 105 U. S. 143 (1881); *Glenn v. Williams*, 60 Md. 93; *Glenn v. Sample*, Alabama, December, 1885. "A company call is but a step in the process of collection, and a court of equity may pursue its own mode of collection, so that no injustice is done to the debtor." *Hatch v. Dana*, 101 U. S. 205 (1879). See also *Myers v. Seeley*, 10 Natl. Bank. Reg. 411; *Sanger v. Upton*, 91 U. S. 56 (1875); *Wilbur v. Stockholders, &c.*, 18 Bank. Reg. 178. Where the corporation, being indebted, has the power to call, and does not choose to exercise it, equity at the instance of creditors will exercise it for them. *Marsh v. Burroughs*, 1 Woods, 463 (1871); *Boeppler v. Menown*, 7 Mo. App. 447 (1885); *Adler v. Milwaukee Patent B. Mfg. Co.* 13 Wis. 57 (1860); *Glenn v. Dodge*, 3 Central Rep. 283 (1886); *Ward v. Griswoldville Mfg. Co.*, 16 Conn. 593 (1844); *Miller's Case*, 54 L. J. (Ch.) 141 (1885); *Henry v. Vermilion & Ashland R. R. Co.*, 17 O. 187 (1848); *Ogilvie v. Knox Ins. Co.*, 22 Hun, 380 (1859); *Curry v. Woodward*, 53 Ala. 371 (1875); *Chandler v. Keith*, 42 Iowa, 99 (1875); *Shackley v. Fisher*, 75 Mo. 498 (1882). The filing of the bill in the suit in equity is equivalent to a call. *Hatch v. Dana*, 101 U. S. 205 (1879); *Thompson v. Reno Sav. Bank, Pac. Rep.*, Jan'y 21, 1886 (Nev.). A late case holds that a decree in a chancery suit is equivalent to a call. *Glenn v. Saxton*, California, January, 1886. Where an assignment is made by the corporation for the benefit of creditors, the statute of limitations begins to run within a reasonable time, even if no call is made. *Glenn v. Dorscheimer*, 24 Fed. Rep. 536 (1885). In

Missouri it has been held that there can be no garnishment of an unpaid subscription until after a call has been made. *Parks v. Heman*, 7 Mo. App. 14 (1879). In New York there are a few *dicta* to the effect that calls by the directors are necessary before unpaid subscriptions can be enforced for the benefit of corporate creditors. *Seymour v. Sturgess*, 26 N. Y. 134 (1862); *Mann v. Pentz*, 3 N. Y. 415 (1850). But the prevailing rule is sustained in *Sagory v. Dubois*, 3 Sandf. Ch. 466 (1846), which says, "The articles, it is true, in effect, require that calls should be made by the directors, and probably the association could not maintain an action at law until such calls were regularly made, but that does not impair the remedy in behalf of the receiver."

² *Glenn v. Saxton*, *supra*; *Crawford v. Rohrer*, 59 Md. 599 (1882). *Contra*, *Paper Co. v. Waples*, 3 Woods, 34 (1877), where the charter prescribed that calls should be only by a three fourths vote of the stockholders.

³ "A chancellor will compel the directors to make the calls required by the charter whenever his aid is invoked by creditors or the representations of creditors." *Germantown Passenger Ry. Co. v. Fidler*, 60 Pa. St. 124 (1869). The three English cases, usually cited on this point, do not hold that a mandamus lies herein. *Queen v. Victoria Park Co.*, 1 Ad. & El. N. S. 544; *Queen v. Ledyard*, Id. 616; *King v. Katharine Dock Co.*, 4 Barn. & Ad. 360 (1832). In the case of *Dalton & Morgantown R. R. Co. v. McDaniel*, 56 Ga. 191 (1876), the court held that a mandamus was unnecessary, on the ground that the remedy by bill was easier and more complete, and that justice would be better administered in this way by an account of all the corporate debts, and of all liabilities of solvent stockholders, taken by a master in chancery. In *Hatch v. Dana*, 101 U. S. 205 (1879),

the writ will not lie for this purpose. The usual procedure to collect unpaid subscriptions is an order of a court of equity made in a suit brought by corporate creditors for the purpose of applying corporate assets to corporate debts.¹

§ 109. *Who has authority to make calls.*—A call, in order to be legal and enforceable, must be made by the proper corporate authorities. Generally the power to make calls is vested in the directors or in the stockholders at large. Unless the charter or a statute makes provisions therefor, the question as to who shall make calls is a question of internal arrangement. If no provisions whatever is made for exercise of the power, it seems to devolve upon the directors under the general principle that they alone have power to manage and superintend the financial matters of the corporation, and to exercise all corporate powers, except those required to be exercised at corporate meetings.² Even though the statute authorizes calls by the stockholders, yet the directors also have the same power.³

§ 110. *Calls by directors.*—Where the power to make calls is vested in the directors, a call made by those who are directors *de facto* will be upheld.⁴ The directors, in whom the power to make

the court says a mandamus "can avail only when there are directors. The remedy in equity is more complete." In *Ward v. Griswoldville Mfg. Co.*, 16 Conn. 593 (1844), the court refused a mandamus because it would enforce the collection of only a few debts. Whereas the remedy in equity would enforce all proportionately.

¹ "Under such circumstances, before there is any obligation upon the stockholders to pay without an assessment and call by the company, there must be some order of a court of competent jurisdiction, or at the very least, some authorized demand upon him for payment." *Seoville v. Thayer*, 105 U. S. 143 (1881). In bankruptcy, it seems, the assignee, by succeeding to all the rights of the corporation, may make a call and enforce it. *Hatch v. Dana*, 101 U. S. 205 (1879).

² The directors may make calls "as they may do all things, except such as are to be done by the shareholders at a general meeting." *Ambergate, N. & B. & E. J. Ry. Co. v. Mitchell*, 4 Ex. Rep. 540 (1849).

³ *Id.* In *Ex-parte Winsor*, 3 Story (C.

C.), 411 (1844), it was held, however, that where the charter gave to the corporation the power to assess stock, it must be exercised exclusively by the stockholders in meeting assembled. On the other hand, in *Rives v. Montgomery, S. P. R. Co.*, 30 Ala. 92 (1857), the court held that stockholders who, by charter, have power to make calls, may delegate that power to the directors.

⁴ "An illegal election of directors cannot be set up in resistance of the payment of stock, but would be a case for a *quo warranto* to oust the illegally elected directors." *Eakright v. Logansport & N. Ind. R. R. Co.*, 13 Ill. 404; *Johnson v. Crawfordsville R. R. Co.*, 11 Ind. 280 (1858); *Fairfield C. T. Co. v. Thorp*, 13 Conn. 173; *Steinmiz v. Versailles R. R. Co.*, 57 Ind. 457 (1877); *Macon R. R. Co. v. Vason*, 57 Ga. 314 (1876); *Atherton v. Sugar, &c., Co.*, 67 Ind. 334 (1879). In the case, however, of *People's Mut. Ins. Co. v. Westcott*, 80 Mass. 440 (1860), a call by directors elected at a meeting held without notice was declared invalid and not enforceable. In England the courts will inquire into the right of directors to

calls is vested, cannot delegate their authority.¹ It is a power, the exercise of which involves a discretion which cannot be delegated to others. A call by a minority meeting of the directors, no quorum being present, is void.²

§ 111. *Assignment of subscription by corporation, before or after call.*—The unpaid and uncalled subscriptions for stock cannot be mortgaged or sold by the corporation. If the transfer by the directors were allowed, “the consequence would be that the discretion which they are bound to exercise would be wholly defeated and put an end to.”³ The power of making calls, being a discretionary one, cannot be transferred to other parties. The transfer is void. The subscribers are bound to pay their subscriptions only when, in the opinion of the proper corporate authorities, or of a court of equity, the money is needed for corporate purposes. This power of ascertaining and determining the extent of the corporate needs being a discretionary power, cannot be transferred or delegated to others. A different rule prevails, however, after a call has been made, but not yet collected, and a transfer of the amount already called is legal and valid.⁴

their office, in cases involving the validity of calls. *Swansea Dock Co. v. Lewien*, 20 L. J. (Ex.), 447 (1851). If the directors were not legally elected, their calls and forfeitures of stock based thereon will be set aside. *Garden Gully U. Q. M. Co., L. R. 1 App. Cas.* 39 (1875).

¹ *Rutland & Burlington R. R. Co. v. Thrall*, 35 Vt. 536 (1863), the court saying: “Where the charter requires the directors to do some specific act, there seems to be a stronger reason why they should be held incapable of delegating such authority than when mere general powers are conferred on them.” See also *Banet v. Alton & Sangamon R. R. Co.*, 13 Ill. 504 (1851); *Pike v. Shore Line*, 68 Me. 445 (1878); *Silver Hook Road v. Greene*, 12 R. I. 164 (1878) where it was delegated to the treasurer; *Mut. Ins. Co. v. Chase*, 56 N. H. 341 (1876), citing authorities; *Monmouth Mut. F. Ins. Co. v. Lowell*, 59 Me. 504 (1871). But where the power is delegated and exercised, the call may be ratified by the directors, and will then be valid. *Read v. Memphis Gayoso Gas Co.*, 9 Heisk. (Tenn.), 545 (1872); *Rutland & B. R. Co. v. Thrall*, 35 Vt. 536 (1863). Although the directors cannot delegate the power to

make a call, yet they may delegate the power “to determine the amount of some of the instalments, and to designate the times of payment.” *Banet v. Alton & S. R. Co.*, *supra*. It is not necessary to allege that the directors were duly elected. *Miller v. Wild Cat G. Road Co.*, 52 Ind. 51 (1875); *Steinmetz v. Versailles & O. T. Co.*, 57 Ind. 457 (1877). But proof must be given that the proper authorities made the call. *N. J. Midland Ry. Co. v. Strait*, 35 N. J. L. 322 (1872).

² *Price v. Grand Rapids & Ind. R. R. Co.*, 13 Ind. 58 (1859); *Hamilton v. Id.*, 13 Ind. 347 (1859).

³ *Ex parte Stanley*, 33 L. J. (Ch.), 535 (1864). To same effect, see *N. J. Midland Ry. Co. v. Strait*, 35 N. J. L. 322 (1872); *Wells v. Rodgers*, 50 Mich. 294 (1883); *Wallingford Mfg. Co. v. Fox*, 12 Vt. 304 (1840); *Bk. of South Australia v. Abrahams*, L. R. 6 P. C. App. 262 (1875); *Hurlbert v. Root*, 12 How. Pr. 511 (1855); *Hill v. Reid*, 16 Barb. 280 (1853); *Hurlbert v. Carter*, 21 Barb. 221 (1855). *Cf. Smith v. Hallett*, 34 Ind. 519 (1870), where the subscription was not for stock, but as a bonus.

⁴ *Humber Ironworks Co.*, 16 Weekly Rep. 474, 667 (1868); *Hills v. Rodgers*,

§ 112. *Interest runs from the time the call is due.*—A subscriber who has failed to pay for his shares according to the terms of his contract, is properly chargeable with interest from the time of the default, and the company cannot be compelled to issue the stock until principal and interest are paid.¹

§ 113. *Stockholders cannot question advisability of calls.*—The necessity or advisability of making a call is a matter which rests exclusively within the discretion of the corporate authorities who have power to make the call.² A stockholder, when sued upon an unpaid call, cannot set up in defense that there was no occasion or use for the money. The call, however, must be for the *bona fide* purpose of raising money for corporate purposes. It must not be for the purpose of enabling the stockholders to use the money paid in to the detriment of the creditors of the failing corporation.³ A court of equity will set aside calls and payments made and managed with a view to discharging the stockholders' liability, and at the same time preventing the proceeds from being applied to the general corporate debts. Equity, however, will not interfere with a call merely because the money received may be diverted by the directors to an act or enterprise beyond the pow-

50 Mich. 294 (1883); *Miller v. Maloney*, 3 B. Monr. (Ky.) 105 (1842), where the call was assigned to the railroad contractor who owed the subscriber for work done; *Downie v. Hoover*, 12 Wis. 174 (1860); *Morris v. Cheney*, 51 Ill. 451 (1869), where, however, it is not clear that a call had been made. A call which has been determined upon, but not definitely made, may be transferred, where it is afterwards duly made by the directors. *Re Sankey Brook Coal Co.*, L. R. 9 Eq. Cas. 721 (1870). A mortgage on all the land, property, and effects of the corporation does not include uncalled subscriptions. *Pickering v. Ilfracombe Ry. Co.*, 37 L. J. (C. P.) 118 (1868); *Lishman's Claim*, 23 L. T. Rep. (N. S.) 759 (1870); *King v. Marshall*, 33 Beav. 565. *Cf. Re Marine M. Co.*, L. R. 4 Eq. Cas. 601 (1867).

¹ *Gould v. Oneonta*, 71 N. Y. 298 (1877); *Rikhoff v. Brown's Rotary, &c.*, Co., 68 Ind. 388. See also *Burr v. Wil-*

cox, 22 N. Y. 551 (1860). *Cf. Stocken's Case*, L. R. 5 Eq. 6 (1867); *Cleveland v. Burnham*, 55 Wis. 598 (1886).

² The question of the necessity for the call "was a matter for the determination of the board of directors." *Chouteau Ins. Co. v. Floyd*, 74 Mo. 286 (1881). "The question whether these necessities demanded the payment of the money was for the directors." *Judah v. American L. S. Ins. Co.*, 4 Ind. 333 (1853).

³ *Habertson's Case*, L. R. 5 Eq. Cas. 286 (1868). Thus, where the amount paid in is immediately paid out to the directors for fees, the transaction is fraudulent, and is set aside. *Syke's Case*, L. R. 13 Eq. Cas. 255 (1871). Nor, on the other hand, can the directors delay calls, in order to enable themselves to transfer their stock and avoid liabilities. *Gilbert's Case*, L. R. 5 Ch. App. 559 (1870); *Preston v. Grand Collier Dock Co.*, 11 Sim. 327 (1840).

ers of the corporation.¹ The corporation cannot contract to postpone indefinitely a call.²

§ 114. *Calls must be impartial and uniform.*—A call cannot be made on a part only of the subscribers. It must be made on all alike, or it will be void.³ The courts will not allow the directors of a company so to proceed as to require some stockholders to pay calls and not to require others to do the same. Any such attempt will be promptly set aside and rectified.⁴

§ 115. *Method of making call.—No formality necessary.*—There are no prescribed or established rules stating how a call shall be made by the corporate authorities authorized to make it. Any act or resolution which, in a court of law, would prove a clear official intent to render due and payable a part or all of the unpaid subscriptions, seems to be sufficient. The call need not indicate when, or to whom, or where payment is required to be made.⁵ These are to be stated in the notice of the call. Mere irregularities are disregarded, and will not invalidate the call.⁶

¹ In the case of *Bailey v. Birkenhead, L. & C. J. Ry. Co.*, 12 Beav. 433 (1850), the court said: It is not within the jurisdiction of courts "to take the accounts and make the inquiries necessary for the purpose of ascertaining whether, under the circumstances to which the company is reduced, and in a continuing concern, it is proper in the due management of the affairs of the company, to raise money by way of calls from the shareholders." Corporate meetings are the places for such complaints. See also *Yetta v. Norfolk Ry. Co.*, 3 De G. & Sm. 293 (1849).

² *McComb v. Credit Mobilier of America, &c.*, 13 Phil. Rep. 468 (1878); *Van Allen v. Ill. Central R. R. Co.*, 7 Bosw. (N. Y.), 515. The last case holding, however, that this principle does not prevent the issue of bonds convertible into stock whenever the stockholder desires.

³ *Pike v. Bangor & Calais S. L. R. R. Co.*, 68 Me. 445 (1878).

⁴ *Preston v. Grand Collier Dock Co.*, 11 Sim. 327 (1840).

⁵ *Fox v. Allensville, C. S. & V. Turnpike Co.*, 46 Ind. 31 (1874); *Andrew v. Ohio & M. R. R. Co.*, 14 Ind. 169 (1860). In the case *Great North of Eng. Ry. Co. v. Biddulph*, 7 Mces. & W. 243 (1840), B. Parke held that the resolution for a call need not state the place of payment nor the person to whom it was payable. See

also *Marsh v. Burroughs*, 1 Woods, 463 (1871), holding that the call need not specify either time or place. See also *Rutland v. Burlington R. R. Co. v. Thrall*, 35 Vt. 536 (1863), that the place need not be stated.

Call made in a new name legally assumed by the corporation, is binding on subscribers who knew of the change of name. *Shackleford v. Dangerfield, L. R.* 3 C. P. 407 (1868).

⁶ Irregularities are no defense. The remedy is to revoke or set aside the call. "Call *in fact* made means that if made, and notice be given, . . . a party shall not wait to take advantage of any irregularity at the trial." *Re British Sugar Ref. Co.*, 3 K. & J. 408 (1857); *Southampton Dock Co. v. Richards*, 2 Railw. Cas. 215, 234 (1840); s. c. 1 Man. & Gr. 448. See also *Shackleford v. Dangerfield, L. R.* 3 C. P. 407 (1868). An error in the call may be corrected and cured by a subsequent call made after the first liability accrued, but before suit. *Phil. & West Chester R. R. Co. v. Hickman*, 28 Pa. St. 318. A director who participated in making the call cannot set up informalities for the purpose of defeating it. *Hays v. Pittsburgh & S. R. R. Co.*, 38 Pa. St. 81 (1860); *Stone v. Great Western Oil Co.*, 41 Ill. 85 (1866). Payment and acquiescence in informality as to one call

The substantial fact must exist that the proper corporate officers voted or declared that payment be required. Hence the elements of a call seem to be that it shall be by the proper persons acting officially; and that a resolution, susceptible of legal proof,¹ be passed, that a certain amount, either the whole or part,² of the subscriptions for stock shall be paid in.

§ 116. *Time, place, amount, and person to whom payable.*—

The time, and place, and person, to whom calls are to be paid need not necessarily be designated or fixed by the persons authorized to make the call.³ These are duties which may be performed by other officers of the corporation, and frequently either the president or treasurer of the corporation performs this work. The time of payment should be reasonable,⁴ as also should be the place. If no place or person to receive payment is designated, it is to be paid to the treasurer at his office.⁵ The amount called need not be made payable in one sum at one time, but may be made due in instalments.⁶

waives it as to another call. *Macon & Augusta R. R. Co. v. Vason*, 57 Ga. 314 (1876).

¹ A call by the directors is valid, although no entry of the resolution is made in the minutes of the directors' meeting. *Hays v. Pittsburgh & S. R. R. Co.*, *supra*. An entry of the resolution, made by the secretary in the book containing the minutes, is sufficient. *Fox v. Allensville C. S. & V. T. Co.*, 46 Ind. 31 (1874). An authorized subsequent call is competent proof of the validity of a previous call. *Barington v. Pittsburgh & S. R. R. Co.*, 34 Pa. St. 358 (1859). The corporate books are competent to prove both the call and the mode of payment. *Barington v. Pittsburgh, &c., R. R. Co.*, *supra*; *Comfort v. Leland*, 3 Whart. (Penn.) 81 (1837).

² The call may be for the whole subscription. *Fox v. Allensville C. S. & V. T. Co.*, 46 Ind. 31 (1874). May be for the whole or for part. *Hann v. Mulberry & Jefferson G. R. Co.*, 33 Ind. 103 (1870); *Stone v. Great Western Oil Co.*, 41 Ill. 85 (1866); *Spangler v. Ind. & Ill. Central R. R. Co.*, 21 Ill. 276 (1859); *Ross v. Lafayette & Indianapolis R. R. Co.*, 6 Ind. 297 (1855). Even though it be expressly provided that only a certain sum shall be assessed at one time, yet several assessments, each one not in excess of the stated sum, may be ordered by a single vote. *Penobscot R. R. Co. v. Dummer*, 40 Me. 172;

Penobscot R. R. Co. v. Dunn, 39 Me. 587 (1855).

³ See *supra*, note 5. The directors themselves may fix the time, place, and manner of payment, even at a meeting subsequent to the meeting ordering a call. The call may be prospective. The directors may order that on a certain date a call payable at a later date shall be made. *Sheffield & Manchester Ry. Co. v. Woodcock*, 7 Mees. & W. 574 (1840). The subscription itself may regulate the time of payment. *N. J. Midland Ry. Co. v. Strait*, 35 N. J. L. 322 (1872); *Roberts v. Mobile & O. R. R. Co.*, 32 Miss. 373 (1856). Even though the statute provides otherwise. *Iowa & Minn. R. R. Co. v. Perkins*, 28 Iowa, 281 (1869).

⁴ *Fairfield County Turnpike Co. v. Thorp*, 13 Conn. 173 (1839). The time between payment of instalments is entirely within the discretion of the directors, there being no provision regulating the subject. *Hall v. U. S. Ins. Co.*, 4 Gill (Md.), 484.

⁵ A resolution of the directors that the instalments should be paid in at the times therein designated, "imports that payments should be made to the treasurer, who is the proper and only officer to receive and keep the moneys of the corporation." *Danbury & Norfolk R. R. Co. v. Wilson*, 22 Conn. 435 (1853).

⁶ *London & North West. Ry. Co. v.*

§ 117. *Notice of calls.—Cases holding it not necessary.*—

There is a wide and irreconcilable difference of opinion among the authorities on the question whether notice of a call must be given to a stockholder before suit can be brought for the collection of the call.

Frequently either the charter, or a statute, or the by-laws of the corporation, require notice to be given, and in such cases notice is, of course, necessary, in order to sustain suit.¹ But where there is no provision in the charter, or statute, or by-laws, or subscription itself, prescribing that notice of calls shall be given to the stockholders, the weight of authority holds that no notice is necessary, and that an action to collect the call may be maintained without averring or proving such a notice.²

§ 118. *Notice of calls.—Cases holding it necessary.*—There is, however, strong authority for the rule that notice of calls

McMichael, 4 Eng. L. & Eq. 459 (1851); Birkenhead L. & C. Ry. Co. v. Webster, Id. 461 (1851); Ambergate Ry. Co. v. Norcliff, Id. 461 (1851); not following Stratford & M. Ry. Co. v. Stratton, 2 B. & Ad. 519 (1831). In Birkenhead L. & E. Ry. Co. v. Webster, as reported in 6 Ex. 277, the court says: "We are unanimously of opinion that a call payable by instalments is good, although debt will not lie for one instalment until all the instalments are due and payable." In Hays v. Pittsburgh & Steubenville R. R. Co., 38 Pa. St. 81 (1860), the court held that the directors by one resolution could call in the balance of the subscriptions, making the call payable in instalments, due at different times. To the same effect see Rutland & Burlington R. R. Co. v. Thrall, 35 Vt. 536 (1863); Lewis' Case, 28 L. T. (N. S.) 396, holding that several assessments, payable at different times, may be made by one vote, where the call was by the court.

¹ In many of the States there exist statutes, very similar in their terms, that notice shall be given of calls, and that in case of non-payment the stock may be forfeited. These statutes have received different interpretations in different States. The usual construction is that the notice required therein refers only to the forfeiture proceedings, and does not necessitate notice before bringing a suit at law for the collection of the call. Smith v. Ind. & Ill. Ry. Co., 12 Ind. 61 (1859); Lake Ontario, Auburn, & N. Y. R. R. Co.

v. Mason, 16 N. Y. 451, 464 (1857). In other States such a statute is construed to require notice before suit. Hughes v. Antietam Mfg. Co. 34 Md. 316 (1870); Granite Roofing Co. v. Michaels, 54 Md. 65 (1880); Dexter & Mason P. R. Co. v. Millerd, 3 Mich. 91 (1854); Ill. River R. Co. v. Zimmer, 20 Ill. 654 (1858), holds that a statute regulating notice of calls does not release the stockholder.

² Wilson v. Wills Valley R. R. Co., 33 Ga. 466 (1863); Eppes v. Miss., Gainesville, & Tuscaloosa R. R. Co., 35 Ala. 33 (1859); Grubb v. Mahoning Nav. Co., 14 Pa. St. 302 (1850); Gray v. Mouongahela Nav. Co., 2 W. & S. (Pa.) 156 (1841); Grubbe v. Vicksburg & Brunswick R. R. Co., 50 Ala. 398 (1878); Eakright v. Logansport & Northern Ind. R. R. Co., 18 Ind. 404; Johnson v. Crawfordville R. R. Co., 11 Ind. 280 (1858); New Albany & Salem R. R. Co. v. McCormick, 10 Ind. 499 (1858); Fisher v. Evansville & C. R. R. Co. 7 Ind. 407 (1856); Ross v. Lafayette & Indianapolis R. R. Co., 6 Ind. 297 (1855); Smith v. Ind. & Ill. Ry. Co., 12 Ind. 61 (1859). In the last case the court says: "These decisions rest upon the ground that the contract to pay by instalments is in effect a promise to pay on demand, and the demand involved in the suit itself was alone sufficient." In New York, since no call is necessary, no notice is necessary. *Of.* Macon & Augusta R. R. Co. v. Vason, 57 Ga. 314 (1876).

must be given before suit is brought for their collection.¹ The reason for this rule seems to accord with sound legal principles and with business expediency. It is a well established principle of law that when the fact or circumstances upon which the performance of a contract depends lies more particularly in the knowledge of the promisee than the promisor, the former must give the latter notice. Hence it would seem that since a subscription is not due absolutely, but only on call, and the time, place, and amount of the call is fixed by persons other than the subscribers, the better and more reasonable rule would be that notice of the call should be required and must be given.

§ 119. *Methods of serving notice of calls.*—The manner and mode of giving notice has given rise to some controversy. Unless provision is expressly otherwise, the notice must be given by handing to the subscriber a written notice, or by informing him orally that the call has been made, giving the amount, time, place, and person to whom payment is to be made.² Where the notice is served, not personally, but by mail, the notice is effective only in case it is actually received.³ Whether it was so received is a question for the jury.⁴ A publication of a

¹ *Wear v. Jacksonville & Savannah R. Co.*, 24 Ill. 593 (1860); *Shangler v. Ind. & Ill. Central R. R. Co.*, 21 Ill. 276 (1859). *Cf. Peake v. Wabash R. R. Co.*, 18 Ill. 88 (1856), holding that notice is unnecessary. In the case *Carlisle v. Cahawba & Marion R. R. Co.*, 4 Ala. (N. S.) 70 (1842), the court says that notice must be given, since "the times, amount of instalments, and manner of payment were all to be prescribed by the president and directors of the corporation, depended upon their volition and action, and consequently was more properly within their knowledge." See also *Scarlett v. Academy of Music*, 43 Md. 203 (1875); *Essex Bridge Co. v. Tuttle*, 2 Vt. 393 (1830); *Rutland & Burlington R. R. Co. v. Thrall*, 35 Vt. 536 (1863); *Miles v. Bough*, 3 Q. B. 845 (1842); *Alabama & Florida R. R. Co. v. Rowley*, 9 Fla. 508 (1861). In *Hughes v. Antietam Mfg. Co.*, 34 Md. 316 (1870), the court says: "To say that it [notice] is unnecessary, because the subscribers, who may be living in different parts of the county, and perhaps the State, are presumed in law to know all that is done by the directors, seems to us to be raising a presumption against the truth itself."

² The notice need not be written. Verbal notification suffices. *Smith v. Tallahassee Plank Road Co.*, 30 Ala. 650-666 (1857). Notice to pay to the treasurer sufficiently indicates the place of payment. It is understood to be at his office. *Muskingum Valley T. Co. v. Ward*, 13 O. 120 (1844). *Contra, Dexter & Mason P. R. Co. v. Millerd*, 3 Mich. 91 (1854). It must be proved to have been sent by authorized persons. *Miles v. Bough*, 3 Q. B. 845 (1842). Notice to various parties in the neighborhood is not sufficient. *New Jersey Midland Ry. Co. v. Strait*, 35 N. J. L. 322 (1872). No particular form of notice is necessary. The only question is "whether the notice gives the shareholder to understand that a call has been made, and that he is required to pay the amount on a given day." *Shackleford v. Dangerfield, L. R.*, 3 C. P. 407 (1868).

³ "Constructive notice by mail is not a personal notice, although in some cases by express statutory provision, it is sufficient to bind parties." *Hughes v. Antietam Mfg. Co.*, 34 Md. 316 (1870).

⁴ A notice of a call may be by mail. If the subscriber denies that he received it, the question is for the jury. *Braddock*

notice in a newspaper is not binding and effectual, unless it be proved that the subscriber, who is sued, actually read the notice as published.¹ A personal notice is sufficient, although the charter, statute, or by-laws provides for notice by publication.² An express promise of the subscriber to pay a call which has been already made, is presumptive evidence that he had notice of that call.³ Notice by publication, given under the authority of a statute, charter, or by-law, must strictly comply with the provisions prescribed as to the time and formalities.⁴

v. Phil., Marlton & Medford R. R. Co., 45 N. J. Law R. 363 (1883). Only the person actually mailing the notice can testify to that fact. *Jones v. Sisson*, 72 Mass. 288 (1856).

¹ In *Alabama & Fla. R. R. Co. v. Rawley*, 9 Fla. 508 (1861), the court says such a mode of notice "might be attended with irreparable injury to innocent parties." See also *dictum*, in *Lake Ontario, Auburn & N. Y. R. R. Co. v. Mason*, 16 N. Y. 451 (1857). In the case of *Schenectady & S. P. R. Co. v. Thatcher*, 11 N. Y. 102 (1854), where the charter prescribed notice by publication or by mail, a director who aided in giving the notices was held to have had personal notice and to be bound. "Personal service of due notice is clearly more advantageous to the defendant, than either an advertisement in a newspaper, or a notice sent by mail." See also *Lexington & West Cambridge R. R. Co. v. Chandler*, 13 Metc. 311.

In the case of *Lincoln v. Wright*, 23 Penn. St. 76 (1854), not a corporation case, Judge Jeremiah Black said that a notice by publication in a newspaper was no notice, unless actually read by the person charged with the notice. "It must be proved that he read it, otherwise it is no stronger than proof that the fact was orally and publicly uttered at a place where he was not present. . . . Where the law requires notice to be given to a party before a liability can be fixed upon him, and the mode of giving such notice is left undetermined, it should be given personally and in fact, and so proved." On the other hand, in *Hall v. U. S. Ins. Co.*, 4 Gill (Md.), 484 (1847), notice of a call by newspaper was held sufficient. The court said: "There is no proportionate object attained by the great inconvenience, labor, and expenses incident to personal notice. The substitution of such newspaper publication in lieu of

personal notice, has so long been an universal usage, and of a notoriety equal to that of a publication of newspapers themselves, that the custom of doing so has become a part of the law of the land." See also *Louisville & E. T. R. Co. v. Meriwether*, 5 B. Monr. (Ky.), 18 (1844), to the same effect, and *dictum* in *Danbury & Norfolk R. R. Co. v. Wilson*, 22 Conn. 435 (1853).

² In the case *Miss. Ouachita & Red River R. R. Co. v. Gaster*, 20 Ark. 455 (1859), the statute prescribed sixty days notice by publication. Actual personal notice was given, and no publication was had. The court sustained the notice and said: "One of the criterions by which to determine whether the requirements of a statute are imperative or merely directory is that those acts which are of the essence of the thing required to be done are imperative, while those which are not of the essence are directory. . . . The giving of sixty days notice is imperative and must be strictly complied with, because it is of the essence of the thing required to be done—the mode of doing so is directory, because not of the essence, and may be either by publication in the manner prescribed by the charter or by actual personal notice." *Cf., semble*, in *Tomlin v. Tonica & Petersburg R. R. Co.*, 23 Ill. 429 (1860).

³ *Miles v. Bough*, 3 Q. B. 845 (1842); *Fairfield County Turnpike Co. v. Thorp*, 13 Conn. 173 (1839).

⁴ Where twenty days notice was required, proof of sending notice is insufficient. Must prove the time of sending. *Cole v. Juliet Opera House Co.*, 79 Ill. 96 (1875). Notice by publication "at least sixty days" is satisfied by one publication sixty days or more before the time of payment. *Muskingum Valley T. Co. v. Ward*, 13 O. 120 (1844); *Marsh v. Burroughs*, 1 Woods, 463 (1871); *Fcx v. Allensville, C. S. & V. T. Co.*, 46 Ind. 31

§ 120. *Demand, waiver, pleadings, &c.*—After notice has been given, no demand is necessary before bringing suit to collect.¹ The subscriber may, by his acts or express agreement, waive the call itself, or informalities in its making, or notice thereof.² It is immaterial that other shareholders have had no notice of the call.³ The proof of calls and of notice, when required, must be clear and complete.⁴ The pleadings in an action on calls must allege the various facts which complete the obligation of the subscriber to pay.⁵

(1874). Fifty-nine days is insufficient where sixty days is prescribed. *Macon & Augusta R. R. Co. v. Vason*, 57 Ga. 314 (1876). The printed notice must be put in evidence. *Rutland & Burlington R. R. Co. v. Thrall*, 35 Vt. 536 (1863). Proof of several insertions is by copy of first insertion and the testimony of the publisher that the others were made. *Unthank v. Henry County T. Co.*, 6 Ind. 125 (1855). The secretary of the corporation cannot, by a certificate, prove publication of notice. *Tomlin v. Tonica & P. R. R. Co.*, 23 Ill. 429 (1860).

¹ *Penobscot R. R. Co. v. Dummer*, 40 Me. 172; *Goodrich v. Reynolds*, 31 Ill. 491 (1863); *Winters v. Muscogee R. R. Co.*, 11 Ga. 438 (1852). *Cf.* *Spangler v. Ind. & Ill. Central R. R. Co.*, 21 Ill. 276 (1859), holding that one demand made for several assessments suffices.

² *Macon & A. R. R. Co. v. Vason*, 57 Ga. 314 (1876). Payment of part of subscription is no waiver of right to have a call made for the balance before payment. *Grosse Isle Hotel Co. v. Ex'rs of L'Anson*, 48 N. J. L. 442 (1881). The vote of a

city to pay a call is no waiver of its invalidity. *Pike v. Bangor & Calais Shore Line R. R. Co.*, 68 Me. 445 (1878). The waiver must be clearly proved. *Rutland & B. R. R. Co. v. Thrall*, 35 Vt. 536 (1863).

³ *Newry & Enniskillen Ry. Co. v. Edmunds*, 2 Ex. Rep. 118 (1848); *Shackelford v. Dangerfield, L. R.*, 3 C. P. 407 (1868).

⁴ *Scarlett v. Academy of Music*, 43 Md. 203 (1875). This case holds also that calls may be proved by reading extracts from the minutes of the directors' meetings, without putting the books in evidence.

⁵ Must allege that the instalments are all due and payable, where several are sued on. *Bethel & Hanover T. Co. v. Bean*, 58 Me. 89 (1870). At common law, the count set out in the declaration, should be not on the contract of subscription, but in *indebitatus assumpsit* for calls, or instalments due. *Peake v. Wabash R. R. Co.*, 18 Ill. 88 (1856). For the customary averments, see *Spangler v. Ind. & Ill. Central R. R. Co.*, 21 Ill. 276 (1859).

CHAPTER VIII.

FORFEITURE OF SHARES FOR NON-PAYMENT.

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| <p>§ 121. The various remedies.</p> <p>122. The remedy by a strict foreclosure.</p> <p>123. The remedy by forfeiture and sale of stock is by statutory authority only.</p> <p>124. The remedy by forfeiture is cumulative.</p> <p>125. When one remedy is exhausted the corporation cannot usually resort to another.</p> <p>126. Ground for contrariety of view as to succession of remedies.</p> <p>127. Forfeiture relieves the shareowner</p> | <p>whose shares are forfeited, from liability to corporate creditors.</p> <p>§ 128. Motives inducing the forfeiture of stock.</p> <p>129. Statutory formalities and general method of forfeiture.</p> <p>130. Notice in cases of forfeiture.</p> <p>131. Notice is not the same thing as forfeiture.</p> <p>132. Tender, by stockholder, before forfeiture.</p> <p>133. Surplus after valid forfeiture, belongs to the corporation.</p> <p>134. Equity will relieve a shareholder from an unauthorized forfeiture.</p> |
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§ 121. *The various remedies.*—Whenever a subscriber fails or refuses to pay for the shares of stock for which he has subscribed, there frequently are open to the corporation, particularly in those jurisdictions where the contract of subscription is interpreted to be a contract to pay, several methods for enforcing the contract. There is the remedy of a close foreclosure, the remedy by forfeiture, and sometimes there is but one—namely, that by the common law action of assumpsit. The last is the general and well nigh universal remedy in most cases. Still another, and, perhaps, the most unusual remedy, is where the corporation, on failure of the subscriber to pay, sues for the amount of the subscription, obtains judgment, and then proceeds to sell the stock under an execution levied to collect the judgment.¹

Again, it has been held that the corporation may have an action at law for breach of contract, the measure of damages being the difference between the value of the stock at the price which the subscriber was to pay and the market value at the date of the refusal to pay.²

¹ Chase v. East Tenn., &c., R. R. Co., 5 Lea, 415.

² Rand v. White Mountains R. R. Co., 40 N. H., 79 (1860).

§ 122. *The remedy by a strict foreclosure.*—A strict foreclosure of shares of stock corresponds, in general, to a strict foreclosure of a mortgage of realty. Like the usual foreclosure of stock by a forfeiture and sale, it is statutory, and can be employed only under the enabling power of the statute. At an early day in New England, a strict foreclosure in these cases was practically the only remedy open to the corporation. Upon such a foreclosure the stock is not sold at public sale, but is taken back into the possession of the corporation itself. It amounts to a statutory cancellation of the contract.¹

§ 123. *The remedy by forfeiture and sale of stock is by statutory authority only.*—In addition to the remedy of an action at law to compel payment of a subscription for stock, there frequently is given to the corporation the right to sell the subscriber's stock for non-payment of his subscription, and apply the proceeds to the payment of that subscription. This is called a forfeiture of the stock. It is not a common-law remedy, and, consequently, can be resorted to by the corporation only when power to make the forfeiture is given to the corporation by statute, or by the act of incorporation.²

The authority to forfeit shares for non payment of the subscription cannot be created by a by-law.³ Such forfeitures are wholly void, and transfers based thereon confer no rights upon the transferee.⁴

¹ Connecticut, &c., R. R. Co. v. Bailey, 24 Vt. 465; Franklin Glass Co. v. White, 14 Mass. 286 (1817). The corporation may then lawfully sell it for less than par. *In re Exchange, &c., Co.* (Ramwell's Case), 50 L. J. (Chan.) 827 (1881). Cf. the leading case, *People v. Albany & Susquehanna R. R. Co.*, 55 Barb. 344 (1869). This strict foreclosure in the case of stock subscribed but not paid for, is frequently called a forfeiture, but it is believed that it is more strictly accurate to apply the term forfeiture to that remedy only which involves a sale of stock for non-payment of subscription. The tendency of the acts of incorporation as well as of the decisions, is to discourage and do away with a strict foreclosure.

² *Westcott v. Minnesota, &c., Co.*, 23 Mich. 145 (1871); *Williams v. Lowe*, 4 Neb. 382 (1876); *Ex parte Barton*, 4 De G. & J. 46; s. c. 28 L. J. (Chan.) 637;

Perrin v. Granger, 30 Vt. 595 (1858); *Clarke v. Hart*, 6 H. of L. Cases, 633 (1858); *Ex parte Fletcher*, 37 L. J. (Chan.) 49; *Stanhope's Case*, L. R. 1 Chan. 161 (1865); *Kelk's Case*, L. R. 9 Eq. 107 (1869); *Campbell's Case*, L. R. 9 Chan. 1 (1873); *Dixon v. Evans*, L. R. 5 H. of L. 606 (1872).

In New York, by statute, this power is conferred both on railway and manufacturing companies. Laws of 1850, ch. 140, § 7; Laws of 1848, ch. 40, § 6.

³ *Master Stevedores' Association v. Walsh*, 2 Daly, 14; *Matter of the Long Island R. R. Co.*, 19 Wend. 37 (1837); s. c. 32 Am. Dec. 429; *Kirk v. Nowill*, 1 Term Rep. 118 (1786). Cf. *Kennebec, &c., R. R. Co. v. Kendall*, 31 Me. 470 (1850); *Cosenback v. Salt Springs National Bank*, 53 Barb. 506.

⁴ *Matter of the Long Island R. R. Co.*, *supra*. Yet where such a power was con-

§ 124. *The remedy by forfeiture is cumulative.*—Frequently when a corporation is authorized by statute to forfeit shares for non-payment of the subscription, the question arises whether the statutory remedy of forfeiture excludes the common-law remedy of an action of assumpsit on the contract. It is the well established rule that it does not. A grant of the power to declare a forfeiture of the shares of a subscriber for non-payment of calls, does not, by implication, deprive the corporation of its common-law right to sue for the unpaid subscription, but the corporate agents may, in their discretion, upon the failure of the subscriber to pay for his stock, either proceed against him by suit to collect the unpaid calls, or may forfeit his shares of stock. The

ferred by a by-law adopted at a meeting of the stockholders, a stockholder whose stock had been declared forfeited under the by-law, and who is shown to have assented to the by-law, will not be heard to question the validity of the forfeiture upon the ground, as it seems, of estoppel, since no rule of law forbids stockholders to enter into an arrangement such as this, which is plainly not contrary to public policy, nor forbidden by the terms of the charter. *Lesseps v. Architects' Co.* 4 La. Ann. 316 (1849).

But in *Perrin v. Granger*, 30 Vt. 595 (1858) it is said that a corporation formed under the general law has no authority, simply by virtue of the provision of the statute, to enforce the collection of assessments by forfeiture unless its constitution or by-laws contain an express provision to that effect, and prescribes the mode of sale, etc.

The corporation cannot, by a by-law, forfeit shares temporarily until assessments or fines shall have been paid. *Adley v. Reeves*, 2 Maule & S. 53 (1849), by Lord Ellenborough; *Cartan v. Father Matthews, &c., Society*, 3 Daly, 20 (1869). *Cf. Pentz v. Citizens Fire, &c., Co.*, 35 Md. 73 (1871); *Kirk v. Nowill*, 1 Term Rep. 118 (1786).

But only the stockholder can object to a forfeiture on the ground that it is by by-law. *Detweiler v. Breckenkamp*, 83 Mo. 45 (1884).

In *Knight's Case*, L. R. 2 Chan. 321 (1867), it appears that in the articles of association of a joint-stock company it was provided that if a shareholder should fail to pay any call, the company might give him notice that in default of pay-

ment within a specified time, his shares would be forfeited; that if the requisitions of any such notice were not duly complied with the shares might be forfeited by a resolution to that effect by the directors; that when any share had been so forfeited, notice of the forfeiture should be given to the delinquent shareowner, and an entry made in the register stating the date of the forfeiture, and that the share should thereupon become the property of the company. *Knight*, a shareholder, being in default in payment of his calls, a notice was sent him in due form that unless he paid the calls by a day named, his shares would be forfeited. The time having elapsed without payment, the secretary of the company made entry in the proper book, on the day following the day named in the notice, that the shares were forfeited, and that they had become the property of the company. It did not appear that there had been any resolution by the directors, or that notice had been sent to *Knight* of the forfeiture. It was argued that if *Knight* had claimed to be a shareholder, the company could not have successfully contested his claim, but it was held that *Knight* having acquiesced, and the company having manifested an evident intention to forfeit his shares, his name could not be placed on the list of contributories as a member of the company on the winding up.

To same effect see *King's Case*, L. R. 2 Chan. 714, 731 (1867); *Brotherhood's Case*, 31 Beav. 365 (1868). Compare *Lyster's Case*, L. R. 4 Eq. 233 (1897); and especially *Houldsworth v. Evans*, L. R. 3 H. of L. 263 (1868), and *Spackman v. Evans*, Id. 171 (1868).

corporation, by such a statute, is given its choice of remedies, and may pursue either. The remedies may be said to be alternative, or, as it is expressed in the decisions, the remedy by forfeiture is merely cumulative.¹

It is to be borne in mind, however, that in the New England States, the right to forfeit stock for non-payment of assessments does not imply a right to the corporation to sue for such assessments, nor does the latter right exist unless it is given by statute or by the express promise of the subscriber.² But where both remedies do exist, the corporation has its election which remedy to pursue.

¹ Delaware, &c., Co. v. Sansom, 1 Binn. 70 (1803); Instone v. Frankfort Bridge Co., 2 Bibb. 576 (1812); Rensselaer, &c., R. R. Co. v. Barton, 16 N. Y. 457 (1857); Lake Ontario, &c., R. R. Co. v. Mason, 16 Id. 451 (1857); Buffalo, &c., R. R. Co. v. Dudley, 14 Id. 336 (1856); Harlem, &c., R. R. Co. v. Seixas, 2 Hall (N. Y. Super. Ct.), 504 (1828); Fort Edward, &c., Co. v. Payne, 17 Barb. 567 (1854); Rensselaer, &c., R. R. Co. v. Wetzel, 21 Id. 56 (1856); Sagory v. Dubois, 3 Sandf. Chan. 466 (1846); Troy, &c., R. R. Co. v. McChesney, 21 Wend. 296 (1839); Herkimer, &c., Co. v. Small, 21 Id. 273 (1839); Ogdensburgh, &c., R. R. Co. v. Frost, 21 Barb. 541 (1856); Northern R. R. Co. v. Miller, 10 Id. 260 (1857); Troy, &c., R. R. Co. v. Tibbits, 18 Id. 297 (1854); Id. v. Kerr, 17 Id. 581 (1854); Union Turnpike Co. v. Jenkins, 1 Caines' Cas. 381 (1803). Compare with this case Townsend v. Goewey, 19 Wend. 424 (1838); Highland, &c., Co. v. McKean, 11 Johns. 98 (1814); Dutchess, &c., Co. v. Davis, 14 Id. 239 (1817); Goshen, &c., Co. v. Hurlin, 9 Johns. 217 (1812); McDonough v. Phelps, 15 How. Prac. 372 (1856); Williams v. Lowe, 4 Neb. 382 (1876); Freeman v. Winchester, 18 Miss. 577 (1848); Hartford, &c., R. R. Co. v. Kennedy, 12 Conn. 499 (1838); Mann v. Cooke, 20 Id. 178 (1849); Essex Bridge Co. v. Tuttle, 2 Vt. 393 (1830); Connecticut, &c., R. R. Co. v. Bailey, 24 Vt. 465; Rutland, &c., R. R. Co. v. Thrall, 35 Id. 536 (1863); New Hampshire, &c., R. R. Co. v. Johnson, 30 N. H. 390 (1855); White Mountains R. R. Co. v. Eastman, 34 Id. 124, 147 (1856); Piscataqua Ferry Co. v. Jones, 39 Id. 491 (1859); Hightower v. Thornton, 8 Ga. 486 (1850);

Hughes v. Antietam, &c., Co., 34 Md. 316 (1870); Beene v. Cahawba, &c., R. R. Co., 3 Ala. 660 (1842); Selma, &c., R. R. Co. v. Tipton, 5 Id. 787 (1843); Gratz v. Redd, 4 B. Mon. (Ky.) 178 (1843); Boston, &c., R. R. Co. v. Wellington, 113 Mass. 79 (1873). [Compare with this case Worcester, &c., Co. v. Willard, 5 Mass. 80 (1809); Andover, &c., Co. v. Gould, 6 Id. 39 (1809); New Bedford, &c., Co. v. Adams, 8 Id. 138 (1811); Chester Glass Co. v. Dewey, 16 Id. 94 (1819); City Hotel v. Dickinson, 6 Gray, 586 (1856); Mechanics, &c., Co. v. Hall, 121 Mass. 272 (1876).] Mexican Gulf, &c., R. R. Co. v. Viavant, 6 Rob. (La.) 305 (1843); New Orleans, &c., Co. v. Briggs, 27 La. Ann. 318 (1875); Greenville, &c., R. R. Co. v. Cathcart, 4 Rich. Law, 89 (1850); Klein v. Alton, &c., R. R. Co., 13 Ill. 514 (1851); Peoria, &c., R. R. Co. v. Elting, 17 Id. 429 (1856); Spangler v. Indiana, &c., R. R. Co., 21 Id. 276 (1859); Kirksey v. Florida, &c., Co., 7 Fla. 23 (1857); Tar River, &c., Co. v. Neal, 3 Hawks (N. C.), 520 (1825); Stokes v. Lebanon, &c., Co., 6 Humph. 241 (1845); South Bay, &c., Co. v. Gray, 30 Me. 547 (1849); Angell & Ames on Corp., §§ 449, 450; Franklin Glass Co. v. Alexander, 2 N. H. 380; s. c. 9 Am. Dec. 92, and the note at pp. 96-104; Thompson's Liability of Stockholders, § 193. For a learned discussion of the general question how far the jurisdiction of a court of equity may be affected by statutes conferring similar jurisdiction upon the courts of law—an inquiry germane to the matter of the present section—see the note to the case of Payne v. Bullard, 23 Miss. 83 (1851), in 55 Am. Dec. 74, 77.

² See Chapter IV.

§ 125. *When one remedy is exhausted the corporation cannot usually resort to another.*—Although, as has appeared, a corporation having the right to declare a forfeiture of shares for non-payment of calls, may generally, at its option, either forfeit the stock or bring an action to collect the amount due, it does not follow that it can forfeit the stock and then bring an action for the unpaid calls, or any part thereof that may remain unsatisfied by the forfeiture. The corporation, when a shareholder is in default, may pursue either the one remedy or the other in its discretion, but it cannot pursue both. It must elect its remedy and then pursue it, and to choose the one is to exclude the other.¹ Such also seems to be the rule in England.² In order, however, to bar the remedy of an action on the contract, the forfeiture must be complete and actual. Consequently a mere threat that a forfeiture will be made if the call be not paid on or before a day named, nor an unsuccessful attempt to sell the shares, will not be sufficient to bar the action.³ So long as the stockholder's right to the shares and to the immunities and emoluments attached to them remain, his obligation to pay is not extinguished.⁴

¹ *Small v. Herkimer, &c., Co.*, 2 N. Y. 330 (1849); reversing *Herkimer, &c., Co. v. Small*, 21 Wend. 273 (1839); s. c. 2 Hill, 127 (1841); *Northern R. R. Co. v. Miller*, 10 Barb. 260, 271 (1851); *Ogdensburg, &c., R. R. Co. v. Frost*, 21 Id. 541 (1856); *Mills v. Stewart*, 41 N. Y. 384 (1869); *Macauly v. Robinson*, 18 La. Ann. 619 (1866); *Athol, &c., R. R. Co. v. Inhabitants of Prescott*, 110 Mass. 213 (1872); *Mechanics, &c., Co. v. Hall*, 121 Id. 272 (1876). With these later Massachusetts cases compare *Andover, &c., Co. v. Gould*, 6 Mass. 40 (1809); *Franklin, &c., Co. v. White*, 14 Id. 286 (1817); *Chester Glass Co. v. Dewey*, 16 Id. 94 (1819); *Ripley v. Sampson*, 10 Pick. 371 (1830); *Cutler v. Middlesex, &c., Co.*, 14 Id. 483 (1833); *Rutland, &c., R. R. Co. v. Thrall*, 35 Vt. 536 (1863); *Macon, &c., R. R. Co. v. Vason*, 57 Ga. 314 (1876); *Ashton v. Burbank*, 2 Dill. 435 (1873).

"It is very plain to us," say the Supreme Court of Vermont, "that it was the intent of the legislature, that the company should not declare the stock forfeited, and after that sue the stockholder. The corpo-

ration can sue or declare the stock forfeited, at their option, and may defer forfeiture till they have exhausted their remedy by suit. If they sue and collect the subscription, the subscriber remains a stockholder. If they declare the stock forfeited, the stockholder loses all previous payments, and ceases to be a member of the corporation. To make him lose his previous payments and his stock, and still be liable for the deficiency which the compulsory sale of his stock fails to pay, would be injustice, unless the charter or general law made such a rule, and the subscriber signed with knowledge of it." *Rutland, &c., R. R. Co. v. Thrall*, 35 Vt. 536, 553 (1863).

² *King's Case*, L. R., 2 Chan. 714 (1867); *Knight's Case*, Id. 321 (1867); *Snell's Case*, L. R., 5 Chan. 22 (1869). Compare *Great Northern, &c., Ry. Co. v. Kennedy*, 4 Exch. 417 (1849).

³ *Macon, &c., R. R. Co. v. Vason*, 57 Ga. 314 (1876).

⁴ *Instone v. Frankfort Bridge Co.*, 2 Bibb, 576. *Of Buffalo, &c., R. R. Co. v. Dudley*, 14 N. Y. 336, 347 (1856).

There is, however, a line of cases in which a contrary rule is contended for, and in which it is said that the forfeiture of shares is like the foreclosure of a mortgage, and that, just as a mortgagee may have judgment against the mortgagor for a deficiency, so may a corporation have its action of assumpsit against a subscriber, whose stock, having been forfeited, has failed to sell for enough to pay his entire indebtedness to the corporation on the subscription.¹ This rule is also held equally applicable to the case of any stockholder who, as transferee of an original subscriber, owns stock which is liable to assessment, and who is in arrears. Such a stockholder is liable, under this rule, for any balance due upon assessments, after applying the proceeds of stock sold for default.²

In this country, as already stated, it is a well established rule in all the States that, where the contract of subscription is in the form of an express promise to pay, the subscriber will be liable personally for the performance of his contract, and may be sued thereon, although a remedy by forfeiture and

¹ *Carson v. Arctic Mining Co.*, 5 Mich. 288; *Danbury, &c., R. R. Co. v. Wilson*, 22 Conn. 435 (1853); *Great Northern Ry. Co. v. Kennedy*, 4 Exch. 417, 425 (1849).

² *Mewinac Mining Co. v. Bagley*, 14 Mich. 501 (1866). *Cf.* *Hartford, &c., R. Co. v. Kennedy*, 12 Conn. 499 (1838); *Brockenbrough v. James River, &c., Co.*, 1 Patton & H. (Va.) 94 (1855); *Mann v. Currie*, 2 Barb. 294 (1848).

It is sometimes provided expressly by statute, or by the charter of the company, that when shares shall have been regularly forfeited and sold, in case the price realized be not sufficient to pay the costs and charges of the sale and the sum due and in arrear to the company, the delinquent stockholder or the original subscriber, or both, and the heirs, executors, or administrators of each or either of them, shall be liable for the payment of the balance. *Brockenbrough v. James River, &c., Co.*, 1 Patton & H. 94 (1855); *Danbury, &c., R. R. Co. v. Wilson*, 22 Conn. 435, 456 (1853); *Great Northern Ry. Co. v. Kennedy*, 4 Exch. 417 (1849); *Mann v. Cooke*, 20 Conn. 178 (1849). But see *Athol, &c., R. R. Co. v. Inhabitants of Prescott*, 110 Mass. 213 (1872); *Allen v. Montgomery R. R. Co.*, 11 Ala. 437 (1847);

Mills v. Stewart, 41 N. Y. 384 (1869). Or that any shareowner, whose shares shall have been forfeited for non-payment of assessments, shall nevertheless be liable to pay to the company all calls owing on such shares at the time of the forfeiture. This seems to be a common provision in the articles of association of English companies. *Creyke's Case*, L. R. 5 Chan. 63 (1869); *Stocken's Case*, L. R. 5 Eq. 6 (1867). But in such a case interest is not collectible. *Stocken's Case*, *supra*. It is, however, otherwise in ordinary defaults. *Gould v. Oneonta*, 71 N. Y. 294 (1877); *Rikhoff v. Brown, &c., Co.*, 68 Ind. 388. In *Great Northern Railway Co. v. Kennedy*, 4 Exch. 417 (1849), in the Court of Exchequer, it was held, construing the statute 8 & 9 Vict., ch. 16, that the 29th section, which enabled the company to declare shares forfeited, was not meant to provide an alternative remedy, but rather that it gave a further security for the payment of calls in the nature of a mortgage or pledge, and that until the company's debt is fully satisfied, it may maintain an action against the defaulting owner for the amount of the calls, or for such part of it as may remain unpaid after sale of the shares.

sale be allowed by the charter of the corporation.¹ In such a case it has been held that, after forfeiture and sale, if there be still a deficiency, the corporation may, upon the ground of the express promise, have its action against the subscriber for the balance due.² But, on the other hand, where the terms of the subscription contain no promise to pay, and the charter only authorizes a forfeiture of the shares for non-payment, it has been held that a close foreclosure of the shares to the company itself will, in such a case, bar a recovery against the subscriber, just as in the more usual case of a forfeiture and sale.³

§ 126. *Ground for contrariety of view as to the succession of remedies.*—If it be conceived that the right of the corporation to forfeit shares for non-payment of calls is analogous to the right of a mortgagee to foreclose his mortgage upon non-payment of the mortgage bond, then the right of the corporation to take a judgment against the subscriber in the event that the stock does not bring enough to pay the debt in full, and the corresponding duty on the part of the corporation to account to the subscriber in case the stock sells for more than the amount of the debt, will

¹ This is the rule, even in New England, since the promise to pay is express. *Boston, &c., R. R. Co. v. Wellington*, 118 Mass. 79 (1873); *City Hotel v. Dickinson*, 6 Gray, 586 (1856); *Buckfield, &c., R. R. Co. v. Irish*, 39 Me. 44 (1854); *Stokes v. Lebanon Turnpike Co.*, 6 Humph. 241 (1845). See also *Instone v. The Frankfort Bridge Co.*, 2 Bibb, 576; also *Hartford, &c., R. R. Co. v. Kennedy*, 12 Conn. 599 (1838), in which a large number of the earlier authorities are collected and critically reviewed.

² *Stokes v. Lebanon Turnpike Co.*, *supra*.

³ *Allen v. Montgomery, &c., R. R. Co.*, 11 Ala. 437 (1847); *Mills v. Stewart*, 41 N. Y. 384 (1869).

In a leading case in New York, *Small v. The Herkimer, &c., Co.*, 2 N. Y. 330 (1849), it was held that the exaction of the forfeiture operates as a rescission or satisfaction of the contract of subscription, and that in consequence there is no remedy over for a deficiency. It was, moreover, said that when a corporation, under such circumstances, exercises its right to forfeit the shares, and the stock is of a greater value than the

whole amount due on the subscription, the subscriber cannot recover the surplus, inasmuch as by the forfeiture his right to the shares is wholly taken away. But the rule seems to be otherwise in England. *Great Northern Ry. Co. v. Kennedy*, 4 Exch. 417 (1849).

In *Giles v. Hutt*, 3 Exch. 18 (1848), where the corporation had, by its deed of settlement, the right, upon non-payment of calls, either to forfeit the shares or bring an action to enforce payment, it was held that the directors, having elected to proceed to judgment against a subscriber for the recovery of the amount of the calls due upon certain shares, could not subsequently and in addition declare the shares forfeited, and that a declaration of forfeiture under such circumstances was wholly void.

Baron Pollock, in the opinion, says: "It appears to us that they might either sue, or instead of suing, that is enforcing payment, they might declare the shares forfeited; but the one being expressly said to be in substitution of the other, we are of opinion that the company cannot resort to both."

be conceded.¹ But if, on the other hand, the right to forfeit be regarded as merely a remedy in the alternative—a statutory right conferred upon the company, of which it may avail itself in its discretion in lieu of the action of assumpsit—a cumulative remedy, to enable an incorporated company the more surely and speedily to realize upon its assets of subscription, then it is clear that by the forfeiture the company must be held to have elected to rescind the contract, and the subscriber to have been thereby released. The company has elected to lose the subscriber as a member and to take the proceeds of the sale of the stock. The subscriber loses what he has paid in, his right to membership and his right to participation in the future profits of the company.

This is the more current, and, it seems, the better view. By the Michigan rule, a subscriber for stock, who has been compelled to pay therefor after the stock itself has been forfeited, will have no stock even after he has paid for it. It has been forfeited. But the contrary rule works no injustice to either party. The corporation cannot complain, since it may pursue either remedy. The subscriber, if he loses his stock, is nevertheless exempt from further payments. If he pays for it, no previous forfeiture can have cut off his right thereto.

§ 127. *Forfeiture relieves the shareholder whose shares are forfeited, from liability to corporate creditors.*—In the absence of fraud and collusion, it is a settled rule that, where a corporation has authority to declare a forfeiture of shares for non-payment of calls, and a forfeiture is regularly declared, such formal declaration puts an end to the liability of the shareowner, and corporate creditors cannot subsequently hold such an expelled or released shareholder liable.² This is the rule, even though the debt was contracted by the company before the stock was forfeited.³ The same principle of law that prevents the corporation from suing on a subscription after the stock has been forfeited, prevents the cor-

¹ This is the rule in the State of Michigan. See *supra*.

² *Allen v. Montgomery R. R. Co.*, 11 Ala. 437, 450 (1847); *Macaulay v. Robinson*, 18 La. Ann. 619 (1866); *Mills v. Stewart*, 41 N. Y. 384 (1869); *Woollaston's Case*, 4 De G. & J. 437; *Ex parte Beresford*, 2 MacN. & G. 197 (1850); *Kelk's Case*, L. R. 9 Eq. 107 (1869);

Dawes' Case, L. R. 6 Eq. 232 (1868); *Snell's Case*, L. R. 5 Chan. 22 (1869). Nor, on the other hand, can the stockholder claim, after the forfeiture, any of the rights of stockholdership. *St. Louis, &c., Co. v. Sandoval, &c., Co.* (Ill. Jan'y, 1886), 12 Am. & Eng. Corp. Cases, 286.

³ *Mills v. Stewart*, *supra*.

porate creditors also from doing the same. But, on the other hand, inasmuch as fraud vitiates all acts into which it enters, a forfeiture of shares by collusion between the shareholders, or any individual shareholder, and the board of directors of the corporation, will not release a shareholder from liability to contribute in the event of the insolvency of the company.¹ In such a case the creditors may invoke the interposition of a court of equity to prevent the consummation of an inchoate forfeiture, or to set aside one already accomplished.²

§ 128. *Motives inducing the forfeiture of stock.*—The forfeiture of stock for non-payment of calls has been justly regarded as a somewhat extreme remedy. In consequence of that view, many controversies have arisen where the validity of the forfeitures has been questioned. Efforts are frequently made to impeach a forfeiture of stock on the ground that the forfeiture was unconscionable and due to a fraudulent intent of the corporate officers. The motives which induce the corporate officers to forfeit a shareholder's stock are important when the validity of the forfeiture is in question, and its validity may be attacked by corporate creditors as well as by the stockholder himself.

Thus it is well settled that the power of forfeiture cannot lawfully be exercised for the purpose of enabling members to escape from their liability on their stock, either to the corporation or its creditors.³

¹ *Slee v. Bloom*, 19 Johns. 456 (1822); *Burke v. Smith*, 16 Wall. 394 (1872); *Mills v. Stewart*, 41 N. Y. 384 (1869); *Walters' Second Case*, 3 De G. & Sm. 244 (1850); *Richmond's Case*, 4 Kay & J. 305 (1858); *Spackman's Case*, 11 Jur. (N. S.), 207; *Stanhope's Case*, L. R. 1 Chan. 161 (1866); *Stewart's Case*, L. R. 1 Chan. 511 (1866); *Gower's Case*, L. R. 6 Eq. 77 (1868). *Cf. Creyke's Case*, L. R. 5 Ch. 63 (1869), where it was held that under the Companies Act a stockholder was liable to corporate creditors, although his stock had been forfeited, the forfeiture being by by-law, not by statute.

² *Germantown, &c., Ry. Co. v. Fitler*, 60 Penn. St. 124 (1869). See also *Grand Rapids Savings Bank v. Warren*, 52 Mich. 557 (1884). The fact that the corporation might have forfeited the stock, if in fact

it did not, is no defense as against the corporate creditors. *Mann v. Currie*, 2 Barb. 294 (1848); *Sagory v. Dubois*, 3 Sandf. Chan. 406 (1846); *Hightower v. Thornton*, 8 Ga. 486, 502 (1850). If a transaction between a shareholder and the directors is irregular, but attempted to be supported by the plea of acquiescence and lapse of time, it is incumbent upon the party setting up such a defense to show that the transaction was fully made known to the general body of the shareholders, and he cannot be heard to insist that it was the duty of the governing body to state the facts of the transaction in question to the other shareholders, i.e. to the corporation, and that he trusted them to do so. *Spackman's Case*, 11 Jur. (N. S.), 207.

³ *Spackman v. Evans*, L. R. 3 H. of L. 171 (1868); *Stanhope's Case*, L. R. 1

It is the duty of the directors, both toward the corporation and its creditors, to enforce full payment of subscriptions for shares, unless they have substantial reasons to believe that the subscriber is not in circumstances which will enable him to pay the sum for which the suit should be brought.¹ Neither should there be a forfeiture for non-payment of assessments, if the subscriber be solvent and the corporation insolvent, so that the real effect of the forfeiture would be prejudicial to creditors.² Nor can a stockholder, by mere abandonment of his shares, forfeit them himself, and thus, by his own act, discharge himself from his obligation on the subscription.³ The power to forfeit shares must be exercised *bona fide*, and for the benefit of the corporation, and with due regard, also, to the claims of the corporate creditors. The corporate management has plainly no right to emasculate the corporation, to destroy its power to act, to give away its assets, or to deprive it in any way of any of its means for accomplishing in full the purpose for which it was incorporated. It is an abuse of their trust for directors to single out some of the subscribers to the cap-

Chan. 161 (1865); *Richmond's Case*, 4 Kay & J. 305 (1858); *Manisty's Case*, 17 Solicitor's Jour. 745; *Gower's Case*, L. R. 6 Eq. 77 (1868); *Ex parte Jones*, 27 L. J. Chan. 666; *Hall's Case*, L. R. 5 Chan. 707 (1870); *Mills v. Stewart*, 41 N. Y. 384 (1869). *Cf. Dixon v. Evans*, L. R. 5 H. of L. 606 (1872); *Lord Belhaven's Case*, 11 Jur. (N. S.), 572 (1865); s. c. 12 L. T. (N. S.), 595 (1867). It is accordingly said that a forfeiture is to be enforced only for its true purpose, with due regard to formalities, and only under circumstances fully justifying a forfeiture. *Clarke v. Hart*, 6 House of Lords Cases, 633 (1858); *Garden Gully, &c., Co. v. McLister*, L. R. 1 App. Cas. 39 (1875); *Sweny v. Smith*, L. R. 7 Eq. 324 (1869); *Gower's Case*, L. R. 6 Eq. 77 (1868). So where the directors of a company made an arrangement with a dissatisfied shareholder, who wished to retire, that on payment by him of a sum of money as consideration, his shares should be declared forfeited for non-payment of a call which had been made, and, in pursuance of this compact, the money was paid and the shares transferred to the company, it was held that the arrangement was *ultra vires*, and in fraud of the other shareholders, and that the widow of the shareholder who had been allowed to retire must, although

twelve years had elapsed, be held liable as a contributory. *Stanhope's Case*, L. R. 1 Chan. 161 (1865). And again, in *Gower's Case*, L. R. 6 Eq. 77 (1868), where certain shares were taken in the joint names of a father and son, and the father was made a director, it was held, where the father having, as he said, discovered that the company had been fraudulently organized, demanded in writing that he and his son be allowed to retire, in pursuance of which demand a resolution was passed by the management forfeiting the shares as if for non-payment; that such so-called forfeiture was void, and that the recalcitrant subscribers were bound.

¹ *Spackman v. Evans*, L. R. 3 H. of L. 171 (1868).

² *Chouteau v. Dean*, 7 Mo. App. 211 (1879). This is also the clear import of the English cases, many of which are cited *supra*. *Cf. Bedford R. R. Co. v. Bowser*, 48 Penn. St. 29 (1864).

³ *Rockville, &c., Turnpike Co. v. Maxwell*, 2 Cranch C. C. 451. *Cf. Mills v. Stewart*, 41 N. Y. 384 (1869). For sundry illustrations of what will or will not justify a forfeiture, see particularly *Sweny v. Smith*, L. R. 7 Eq. 324 (1869); *Stocken's Case*, L. R. 3 Chan. 412 (1867); *Count Pahlen's Case*, L. R. 9 Eq. 107 (1869); *Thomas' Case*, L. R. 13 Eq. 437.

ital stock and release them from their liability, and this equally without regard to whether the motive be to injure the shareholder released, or to prevent corporate creditors from making their claims, or to shield the shareholder from the full measure of any part of his just responsibility as a subscriber.¹

§ 129. *Statutory formalities and general method of forfeiture.*—The general method of forfeiting shares for non-payment of calls is usually prescribed in detail by the statute authorizing the forfeiture. The power can exist only by virtue of an express statutory provision, and when it is conferred upon a corporation, the steps to be pursued in the exercise of the power are usually prescribed also. In the earlier cases there may be observed some tendency to hold that a substantial, in distinction from a strict, compliance with the requirements of the statute is all that is necessary to a valid forfeiture.² But in later cases, English³ and American,⁴ it is plainly declared, and it may be taken as a settled rule, that the validity of the forfeiture and sale of the shares of a subscriber in arrears, depends upon a strict and formal compliance with the requirements of the enabling statute.⁵

¹ Bedford R. R. Co. v. Bowser, 48 Penn. St. 29 (1864), and the English cases which have been cited in this section *supra*.

² Catchpole v. Ambergate, &c., Ry. Co., 1 Ellis & B. 111 (1852); Naylor v. South Devon Ry. Co., 1 De G. & Sm. 32 (1846). Cf. Howbeach, &c., Co. v. Teague, 5 Hurl. & N. 151 (1860); Nolan v. Arabella, &c., Co., 6 W. W. & A. B. (Australian), 38.

³ Clarke v. Hart, 6 House of Lords Cases, 633 (1858); Johnson v. Lyttle's Iron Agency, 46 L. J. (Chan.) 786 (1877). Cf. Knight's Case, L. R., 2 Chan. 321 (1867); Garden Gully, &c., Co. v. McLister, L. R., 1 App. Cas. 39 (1875); London & B. Ry. Co. v. Fairclough, 2 Mann & G. 674 (1841).

⁴ Portland, &c., R. R. Co. v. Graham, 11 Metc. 1 (by Shaw, C. J., 1846); Germantown, &c., Ry. Co. v. Fittler, 60 Penn. St. 124 (1869); Eastern, &c., Plank Road Co. v. Vaughan, 20 Barb. 155 (1855); York, &c., R. R. Co. v. Ritchie, 40 Me. 425 (1855); Lewey's Island R. R. Co. v. Bolton, 48 Id. 451 (1860); Downing v. Potts, 23 N. J. (Law), 66; Matter of the Long Island R. R. Co., 19 Wend. 37 (1837); Mitchell v. Vermont Copper Mining Co., 40 N. Y. Super. Ct. 406 (1876);

Occidental, &c., Assoc. v. Sullivan, 62 Cal. 394 (1882). Cf. Johnson v. Albany, &c., R. R. Co., 40 How. Prac. 193 (1870); Rutland, &c., R. R. Co. v. Thrall, 35 Vt. 536 (1863); Perrin v. Granger, 30 Id. 595 (1858).

⁵ Accordingly we find it said, that powers of forfeiture are *strictissimi juris*, that they must exist by statute, or the clear terms of a contract, that they are penal in their nature and must, therefore, be strictly construed. Garden Gully, &c., Co. v. McLister, L. R., 1 App. Cas. 39 (1875). And that unless all the conditions precedent have been duly fulfilled, *modo et forma*, the forfeiture may be set aside. Garden Gully, &c., Co. v. McLister, *supra*; Germantown, &c., Ry. Co. v. Fittler, 60 Penn. St. 124 (1869). In the opinion in this case, Sharswood, J., said: "We must look to the charter for the power of the directors to forfeit the stock. No doubt the power given must be strictly pursued, and if any restrictions or limitations there provided have been disregarded, the alleged act of forfeiture must be declared invalid. This is so for the special reason that it is one of those forfeitures against which, if regular, equity does not relieve," citing 1 Redfield on Railways, 214. When the cor-

Thus a sale of the shares at private sale, when a sale by public auction was prescribed, has been held to invalidate the forfeiture.¹ There must be a properly constituted board of directors to declare a forfeiture of shares.² Inasmuch as the right of forfeiture is purely a statutory right, there are, aside from the statutes, no definite common law rules to regulate the matter of declaring and effecting a forfeiture. It is, however, held, in general, that, in the absence of statutory provisions as to order or details, the mode of forfeiture must be reasonable and just.³ The forfeiture, under such circumstances, may be regularly effected by a resolution of the board of directors, ordering a sale of all stock on which assessments shall remain unpaid at a day named in the future.⁴

It is a well established rule also, that a forfeiture of shares, where the forfeiture was irregular or defective in its form, or even where there was no power to forfeit, is not void, but voidable, and that by subsequent knowledge and acquiescence, the

poration has power to sell the stock of a subscriber for the failure to pay each or any call as it is made, it will lose its right to a remedy by forfeiture and sale, by failing to sell the stock at the first default and waiting until all the calls are made. *Stokes v. Lebanon, &c., Co.*, 6 *Humph.* 241 (1845). It is doubtful, however, whether this is good law, as a general rule. The interest of both parties is frequently best subserved by delay, during which time the subscriber may be able to pay up.

¹ *Lewey's Island R. R. Co. v. Bolton*, 48 *Me.* 451 (1860), as to what is, in general, sufficient to satisfy the requirements of the rule that powers of forfeiture are to be construed strictly and exercised or pursued strictly. See *Giles v. Hutt*, 3 *Exch.* 18 (1848); *Catchpole v. Ambergate, &c., Ry. Co.*, 1 *Ellis & B.* 111 (1852); *Birmingham, &c., Ry. Co. v. Locke*, 1 *Q. B.* 256 (1841); *Graham v. Van Dieman's Land Co.*, 1 *Hurl. & N.* 541 (1856); *Sweny v. Smith, L. R.*, 7 *Eq.* 324 (1869); *Stocken's Case, L. R.*, 3 *Chan.* 412 (1867); *Count Pahlen's Case, L. R.*, 9 *Eq.* 107 (1869); *Thomas' Case, L. R.*, 13 *Eq.* 437; *Gower's Case, L. R.*, 6 *Eq.* 77 (1868). It has, however, been held in an English case—*In re North Hallenbeagle Mining Co., Knight's Case, L. R.*, 2 *Chan.* 321 (1867); *s. c.* 15 *L. T. (N. S.)* 546 (1869)—that when it is a matter of mere form, rather than of substance that

has not been strictly followed, in proceedings to forfeit shares, the forfeiture will not necessarily be thereby invalidated.

² *Garden Gully, &c., Co. v. McLister, L. R.*, 1 *App. Cases*, 39, 55 (1875).

³ *Rutland, &c., R. R. Co. v. Thrall*, 35 *Vt.* 536 (1863); *Mitchell v. Vermont Copper Mining Co.*, 67 *N. Y.* 280 (1876).

⁴ *Rutland, &c., R. R. Co. v. Thrall*, 35 *Vt.* 536 (1863). *Acc. Woollaston's Case*, 4 *De G. & J.* 437. Under such a resolution a sale of the stock is not necessary to complete the forfeiture where the effect of the forfeiture is to release the stockholder from any future liability, and where he is not entitled to the surplus, if any there be, after sale. *Rutland, &c., R. R. Co. v. Thrall, supra*. It is, however, said elsewhere that a general resolution, not specifying the stock which is forfeited, but merely assuming to forfeit any and all stock whose owners are in arrears, does not effect a valid forfeiture. *Johnson v. Albany, &c., R. R. Co.*, 40 *How. Prac.* 193 (1870). When, after default made in the payment of assessments, notice is given by the corporation that the shares of owners in arrears will be forfeited unless full payment of what is due be made by a day named, there is a presumption that the subsequent proceedings of the company, looking to perfecting the forfeiture, are valid and regular. *Knight's Case*, 15 *L. T. (N. S.)* 546 (1867).

shareholder and the company are alike estopped to deny its validity.¹

§ 130. *Notice in cases of forfeiture.*—A notice to the delinquent subscriber, that his shares will be forfeited at a day named, is generally requisite to the validity of a forfeiture. The subscriber is entitled to full knowledge of the fact that unless he pays up within a specified time, he will lose his stock. The requirements of the statute or charter, with respect to the contents of the notice, and the length of time which is to elapse between the notice and the forfeiture, must all be strictly complied with. Notice of a forfeiture is generally a condition precedent to the validity of that forfeiture, and unless the notice be in all respects regular and conformable to the law authorizing the forfeiture, the forfeiture itself will be invalid and void.² It is accordingly held, that the notice must state correctly the amount due for non-payment of which the stock is to be forfeited.³ The time also within which payment

¹ King's Case, L. R., 2 Chan. 714, 731 (1867); Woollaston's Case, 4 De G. & J. 437; Webster's Case, 32 L. J. Chan. 135 (1863); Knight's Case, L. R., 2 Chan. 321 (1867); Kelk's Case, L. R., 9 Eq. 107 (1869); Austin's Case, 24 L. T. (N. S.) 932 (1871); Pendergast v. Turton, 1 Y. & C. (Ch.) 98 (1841). Cf. Lyster's Case, L. R., 4 Eq. 233 (1867); Campbell's Case, L. R., 9 Chan. 1 (1873); Teasdale's Case, L. R., 9 Chan. 54 (1873); Phosphate, &c., Co. v. Green, L. R., 7 C. P. 43 (1871); Houldsworth v. Evans, L. R., 3 H. of L. 263 (1868); Spackman v. Evans, L. R., 3 H. of L. 171 (1868); Brotherhood's Case, 31 Beav. 365 (1862); Lesseps v. Architects Co., 4 La. Ann. 316 (1849). And see also Matter of Long Island R. R. Co., 19 Wend. 37 (1837); Kennebec, &c., R. R. Co. v. Kendall, 31 Me. 470 (1850); Kirk v. Nowill, 1 Term Rep. 118 (1786); Lindley on Partnership, 744 *et seq.*; Garden Gully, &c., Co. v. McLister, L. R., 1 App. Cas. 39, 55 (1875), holding that mere laches does not, of itself, disentitle the holder of shares to equitable relief against an invalid declaration of forfeiture.

² Heaston v. Cincinnati, &c., R. R. Co., 16 Ind. 275 (1861); Lexington, &c., R. R. Co. v. Chandler, 13 Mete. 311 (1847); Lewey's Island R. R. Co. v. Bolton, 48 Me. 451 (1860); Rutland, &c., R. R. Co. v. Thrall, 35 Vt. 546 (1863); Lake On-

tario, &c., R. R. Co. v. Mason, 16 N. Y. 451 (1854); Sands v. Sanders, 26 Id. 239 (1863); Mississippi, &c., R. R. Co. v. Gaster, 20 Ark. 455 (1859); Hughes v. Antietam, &c., Co., 34 Md. 317 (1870); Johnson v. Lyttle's Iron Agency, 46 L. J. (Chan.) 786 (1877); Cockerell v. Van Dieman's Land Co., 26 L. J. (C. P.) 203; Watson v. Eales, 23 Beav. 294 (1856); Birmingham, &c., Ry. Co. v. Locke, 1 Q. B. 256 (1841); Knight's Case, L. R., 2 Chan. 321 (1867). Cf. Eppes v. Mississippi, &c., R. R. Co., 35 Ala. 33 (1859); Bangs v. Duckinfield, 18 N. Y. 592 (1859); Schenectady, &c., R. R. Co. v. Thatcher, 11 Id. 102 (1854); Harlaem, &c., Co. v. Seixas, 2 Hall (N. Y. Super. Ct.), 504 (1829); Mitchell v. Vermont Copper Mining Co., 40 N. Y. Super. Ct. 406 (1876); New Albany, &c., R. R. Co. v. McCormick, 10 Ind. 499 (1857).

³ So where the notice stated that unless the amount of a certain call, together with lawful interest from the date of the call, was paid on or before a certain day, the shares would be liable to forfeiture, it was held that, as interest was only payable from the day fixed for payment, and not from the date of the call, the notice was irregular, and that a forfeiture founded on a non-compliance with such a notice was bad. Johnson v. Lyttle's Iron Agency, 46 L. J. (Chan.) 786 (1877).

is to be made must be accurately stated,¹ and also the place where the sale is to be made.² The mode of giving notice of a contemplated forfeiture of stock is generally specified in the statute authorizing the forfeiture.³

§ 131. *Notice is not the same thing as forfeiture.*—A notice of a probable or certain forfeiture in the future, which may perhaps be described as a threat of forfeiture, is not forfeiture, and does not become forfeiture merely by non-payment of the call or assessment within the time specified in the notice.⁴ A forfeiture

¹ A notice that the stock will be forfeited "on Monday, the 9th," when in point of fact the 9th comes on Friday, is not a sufficient notice. *Watson v. Eales*, 23 Beav. 294 (1856).

² Accordingly a notice in all other respects regular, which does not state the place of sale, is insufficient, although it name the day of sale, and the auctioneer, who was and had long been an auctioneer in the place at which the notice was dated. *Lexington, &c., R. R. Co. v. Staples*, 71 Mass. 520 (1855) (by Shaw, C. J.). In the absence of a statutory provision as to time, it is said that three days notice of the time and place of the sale of shares for non-payment of assessments is too short and unreasonable, where the owner of the shares lived at a distance in another State. *Lexington, &c., R. R. Co. v. Staples, supra*. In *Rutland, &c., R. R. Co. v. Thrall*, 35 Vt. 536 (1863), a thirty days notice is said to be sufficient and reasonable. And where the charter provided that notice of an assessment should be given to the subscriber thirty days before the order of the directors to sell the shares, a notice thirty days before the sale was held insufficient. *Lewey's Island R. R. Co. v. Bolton*, 48 Me. 451 (1860); *Louisville, &c., Turnpike Co. v. Meriwether*, 5 B. Mon. 13. A printed notice in designated newspapers, published in cities where the subscribers reside, is good. *Louisville, &c., Turnpike Co. v. Meriwether, supra*.

³ In Mississippi, *Ouachita & Red River R. R. Co. v. Gaster*, 20 Ark. 455 (1859), it is said that the mode of giving a notice in these cases is directory, rather than mandatory, and that where the charter provided that notice be given in certain newspapers, a personal notice would be sufficient. *Acc. Knight's Case*, L. R., 2 Chan. 321 (1867). So, where a by-law provided for notice by letter, seasonably

put into the mail, it was held that this by-law was only directory to the treasurer, and not a condition precedent, and that a written notice, signed by the treasurer, in other respects sufficient and regular, would not be invalidated merely because it was delivered to the owner of the shares or left at his dwelling-house instead of being deposited in the mail, when it appeared that it was received by him as soon as he was entitled to receive it by mail. *Lexington, &c., R. R. Co. v. Chandler*, 13 Metc. 311 (1847). But see *Lewey's Island R. R. Co. v. Bolton*, 48 Me. 451 (1860). In general, as to the effect of such a notice left at one's residence or place of business, or where similar notices have previously been left, and been duly received, but which, for some reason, never reach the person for whom they are intended, see *Cockerell v. Van Dieman's Land Co.*, 26 L. J. (C. P.) 203. *Cf. Birmingham, &c., Ry. Co. v. Locke*, 1 Q. B. 256 (1841); *Graham v. The Van Dieman's Land Co.*, 1 Hurl. & N. 541 (1856) (a case in which notice was held properly served on a bankrupt though his effects were in the hands of an assignee). See also *South Staffordshire Ry. Co. v. Burnside*, 5 Exch. 129 (1850).

⁴ *Macon, &c., R. R. Co. v. Vason*, 57 Ga. 314 (1876); *Bigg's Case*, L. R., 1 Eq. 309 (1865); *Cockerell v. Van Dieman's Land Co.*, 26 L. R. (C. P.) 203; *Water Valley Mfg. Co. v. Seaman*, 53 Miss. 655 (1876), where only a threat was made. But see *contra, Knight's Case*, L. R., 2 Chan. 321 (1867). It is said that mere non-payment of calls, where the corporation has power to forfeit for non-payment, produces only an inchoate forfeiture, which is not complete until due notice thereof is given to the delinquent owner of the stock, and the shares have been duly declared forfeited at a regular and lawful meeting of the corporation.

§ 133.] FORFEITURE OF SHARES FOR NON-PAYMENT. [CH. VIII.

is void if declared for the non-payment of assessments, when all or any one of the assessments were illegal or unauthorized.¹

§ 132. *Tender, by stockholder, before forfeiture.*—Where the amount due on a subscription for non-payment of which a forfeiture is about to take place, is tendered to the proper officer of the corporation at any time before the sale actually takes place,² the forfeiture is thereby prevented. Thus, in *Walker v. Ogden*,³ it has been held that where the articles of association do not provide an express mode in which stock is to be forfeited, a valid forfeiture cannot be made without the decree of a court of equity; that after such a foreclosure there is a right to redeem; and that, where the subscriber had given security for the payment of his assessments overdue, and subsequently paid the amount due, principal and interest, the corporation would be compelled to make and deliver to him the proper certificate, and to recognize him as a stockholder.

§ 133. *Surplus after valid forfeiture, belongs to the corporation.*—Upon a sale of the stock forfeited, if the amount realized is more than the debt due the corporation, the surplus belongs to

Cockerell v. Van Dieman's Land Co. supra. But on the other hand it is argued that the notice is not of the essence of the forfeiture, while the non-payment is; that the forfeiture is effected and consummated when the time has elapsed within which payment of the assessment ought to have been made, without a valid payment, and that the provision as to sending a notice may well be regarded mandatory. *Knight's Case*, L. R., 2 Chan. 321 (1867). In *Austin's Case*, 24 L. T. (N. S.) 932 (1871), it is said that a corporation, after forfeiting shares, cannot set the forfeiture aside, *ex mero motu*, and hold the owner liable as a subscriber, on the ground that the notice given him was irregular, or faulty, or insufficient. It is for the subscriber alone to raise that objection to the validity of the forfeiture. But the facts involving the matter of notice may be of such a nature that even after forfeiture, the owner of the shares will not be heard to allege that his shares have been forfeited, nor the corporation be precluded from treating him as a stockholder. *Birmingham, &c., Ry. Co. v. Locke*, 1 Q. B. 256 (1841).

¹ *Stoneham, &c., R. R. Co. v. Gould*, 2

Gray, 277 (1854); *Lewey's Island R. R. Co. v. Bolton*, 48 Me. 451.

² *Sweny v. Smith*, L. R., 7 Eq. 324 (1869); *Walker v. Ogden*, 1 Biss. 287 (1859). In *Mitchell v. Vermont Copper Mining Co.*, 67 N. Y. 280 (1876), it appears that the directors of the mining company, having imposed an assessment upon the shares, advertised those of M., for sale for non-payment thereof, M. being in default. Prior to the sale, however, M. tendered to the president of the company, at its office, during business hours, his check for the amount due, which without any objection as to the form or amount was declined, and the stock was subsequently sold to the president. M. repeatedly thereafter offered to the company and to the president the amount of the assessment and the charges and expenses of the sale, but without being able to recover his stock. In an action to set aside the sale and to prevent a transfer to the purchaser, the court held the tender good, the pretended forfeiture of the shares inequitable and void, and that the plaintiff was entitled to equitable relief.

³ 1 Biss. 287 (1859).

the corporation.¹ The purchaser at the forfeiture sale, if the stock has been only partially paid for, must pay the instalments due and to come due, and if he fail to make these payments the stock must be sold again.²

§ 134. *Equity will relieve a shareholder from an unauthorized forfeiture.*—The shareowner himself, as well as a corporate creditor, may, in a proper case, invoke the aid of a court of chancery when his shares have been forfeited in an unauthorized, or an unlawful manner. Usually in such a case, the shareholder may, by bill in equity, obtain a decree annulling the forfeiture.³ So also equity will sometimes set aside a forfeiture upon purely equitable grounds, as, for example, where a forfeiture was declared for non-payments of calls, which, it was shown, were not paid, because the shareholder died, and no administrator had been appointed until the time for payment had fully elapsed.⁴ But it seems that the weight of authority is to the effect that a forfeiture of shares, lawful and regular, for non-payment of assessments, is one of those forfeitures from which equity will

¹ *Small v. Herkimer, &c., Co.*, 2 N. Y. 330 (1849). But compare cases on p. 129, and see *Sturges v. Stetson*, 1 Biss. 246 (1858).

² *Sturges v. Stetson*, 1 Biss. 246, 251 (1858).

³ *Sweny v. Smith*, L. R., 7 Eq. 324 (1869); *Mitchell v. Vermont, &c., Co.*, 67 N. Y. 280 (1876); *Adley v. Whitsable Co.*, 17 Ves. 315 (1810, by Lord Eldon); *Sloman v. Bank of England*, 14 Sim. 475 (1845); *Taylor v. Midland Ry. Co.*, 28 Beav. 287 (1860); s. c. 29 L. J. (Chan.) 731. Cf. *Telegraph Co. v. Davenport*, 97 U. S. 369 (1878); *Germantown, &c., Ry. Co. v. Fidler*, 60 Penn. St. 124 (1869); *Pratt v. Taunton, &c., Co.*, 123 Mass. 110 (1877); *Lowry v. Commercial, &c., Bank*, Taney C. C. 310; *Sewall v. Boston, &c., Co.*, 4 Allen, 277 (1862); *Chew v. Bank of Baltimore*, 14 Md. 299 (1859); *Pollock v. The National Bank*, 7 N. Y. 274 (1852); *Weaver v. Barden*, 49 Id. 286 (1872); *Cohen v. Gwynn*, 4 Md. Chan. 357 (1848); *Naylor v. South, &c., Ry. Co.*, 1 De G. & S. 32 (1846); *Norman v. Mitchell*, 5 De G., M. & G. 648; *Johnson v. Renton*, L. R., 9 Eq. 181 (1870); *Cottam v. Eastern, &c., Ry. Co.*, 1 Johns. & H. 243 (1860); *Swan v. North British, &c., Co.*, 7 Hurl. & N. 603; *Dalton v. Midland Ry. Co.*, 22 Eng. L. & Eq. 452 (1852); *Davis v. Bank*

of England, 2 Bing. 393; *Hilgard v. South Sea Co.*, 2 P. Wms. 76 (1722); *Ashby v. Blackwell*, 2 Eden, 299 (1765). Thus a forfeiture of shares for non-payment of calls declared at a meeting held out of the State in which the company was incorporated, the meeting being in consequence an unlawful meeting, may be set aside upon a proper application to a court of chancery, at any time within the period prescribed by the statute of limitations for bringing an action for conversion. *Ormsby v. Vermont, &c., Co.*, 56 N. Y. 623 (1874). An unlawful attempt to forfeit shares is, it is said, equivalent to a conversion of them. *Freeman v. Harwood*, 49 Me. 195 (1859); *Van Dieman's Land Co. v. Cockerell*, 1 C. B. (N. S.) 732.

⁴ *Glass v. Hope*, 16 Grant (Up. Can. Chan.) 420 (1869). In one case, the extreme ground has been taken that, in any event, a court of equity may grant relief by ordering that upon payment in full of the amount due principal and interest, the complainant shall be allowed to redeem. *Walker v. Ogden*, 1 Biss. 287. This, however, is very doubtful law, since a court of equity rarely grants relief from a forfeiture clearly and legally imposed. *Vatable v. New York, L. E. & W. R. R. Co.*, 96 N. Y. 49 (1884).

not, except in very exceptional cases, afford relief.¹ When the shareholder has lost his shares by an irregular or unlawful forfeiture, his suit should be for the recovery of his shares, and not for an undivided interest in the property of the company.² Acquiescence or delay, as we have seen, on the part of the shareholder, will usually bar his right in a court of equity, to have such a forfeiture as we have considered above, set aside.³

¹ *Sparks v. The Company of Proprietors of the Liverpool Water Works*, 13 Ves. 428 (1807); *Germantown, &c., Ry. Co. v. Fitler*, 60 Penn. St. 124 (1869). Equity will not relieve from such forfeitures, because to do so would, it is said, be in contravention of the direct expression of the legislative will. *Small v. Herkimer, &c., Co.*, 2 N. Y. 330, 340 (1849). Neither can a shareowner have a forfeiture set aside, merely because the calls, which he refused to pay, were for the purpose of paying debts which the company would not have owed but for the previous misappropriation of the corporate funds of the trustees. *Marshall v. Golden Fleece, &c., Co.*, 16 Nev. 156. See *Wilkins v. Thorne*, 60 Md. 253 (1883); *Petersborough R. R. Co. v. Nashua, &c., R. R. Co.*, 59 N. H. 385.

² *Smith v. Maine Boys Tunnel Co.*, 18 Cal. 111 (1861). In the opinion herein the court says: "The plaintiff has mistaken his remedy. If his stock has

been improperly sold, he may maintain an action for its recovery, but he cannot sue the corporation for a specific interest in the corporate property. It appears that he was one of the original incorporators, and that the property in question has been held as corporate property from the time the corporation was formed. Under these circumstances he should not, we think, be permitted to question the title of the corporation." The suit to set aside the forfeiture must be brought in the State where the corporation is domiciled. *North State, &c., Co. v. Field*, 64 Md. 151 (1885); *Sudlow v. Dutch R. R. Co.*, 21 Beav. 43 (1855).

³ *Vide* § 129, *supra*. It will, moreover, sometimes be found that a general statute, or the charter of the corporation, fixes or limits the time within which a shareholder will be allowed to make such an application to a court of chancery. Thus in California such an application must be made within six months.

CHAPTER IX.

PAROL AGREEMENTS AND FRAUDULENT REPRESENTATIONS INDUCING SUBSCRIPTIONS FOR STOCK.

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§ 135. *Scope of the subject.*—Parol agreements and fraudulent representations inducing subscriptions to stock have been a prolific source of litigation, both in this country and in England. As a defense to actions brought for the collection of subscriptions, and as the basis of suits in equity to set aside subscriptions and compel a repayment of money already paid on such subscriptions, the agreements and representations made to induce persons to subscribe for stock have given rise to intricate principles of law peculiar to this subject.

§ 136. *Definitions.*—A parol agreement includes all representations and stipulations made before or at the time of subscribing, but not included in the written subscription, whereby the corporation is to do something or refrain from doing something in the future. A fraudulent representation, on the other hand, is a statement as to past acts or existing facts, or the omission of such a statement, which amount to a fraud on one who, relying thereon, subscribes to the stock of the company. Difficulty sometimes

arises in determining whether a statement by a corporate agent inducing a subscription is merely a parol agreement or is a fraudulent representation. This question is one which must be decided first of all, since the rules of law applicable to parol agreements, as a defense to an action on a subscription, differ greatly from those applicable to fraudulent representations.

§ 137. *Parol agreements.*—Where a subscription contract is absolute on its face, it is well settled, both in equity and at law, that parol evidence of previous or contemporaneous negotiations, stipulations, terms, or agreements, is not admissible except for the purpose of proving that the parties, at the time of consummating the agreement, intended and understood that such terms and stipulations would be incorporated, but omitted the same by accident, fraud, or mistake.¹ This rule, forbidding the introduction of parol evidence to explain, contradict, or vary a written instru-

¹ *Piscataqua Ferry Co. v. Jones*, 39 N. H. 491 (1859); *Kennebec & Portland R. R. Co. v. Waters*, 34 Me. 369 (1852); *Cincinnati Union & Ft. Wayne R. R. Co. v. Pearce*, 28 Ind. 502 (1867); *Scarlett v. Academy of Music*, 46 Md. 132 (1876); *Dill v. Wabash Valley R. R. Co.*, 21 Ill. 91 (1859); *East Tenn. & Va. R. R. Co. v. Gammon*, 5 Sneed. (Tenn.) 567 (1858); *Corwith v. Culver*, 69 Ill. 502 (1873); *Jack v. Naher*, 15 Iowa, 450 (1863); *Thornburgh v. Newcastle & D. R. R. Co.*, 14 Ind. 499 (1860); *Gelpeke v. Blake*, 15 Iowa, 387 (1863), holding that it is immaterial that the agent acted in good faith. *Johnson v. Pensacola & Ga. R. R. Co.*, 9 Fla. 299 (1860); *Miss. O. & R. R. Co. v. Cross*, 20 Ark. 443 (1859); *Ridgefield & N. Y. R. R. Co. v. Brush*, 43 Conn. 86 (1875); *Phoenix Warehousing Co. v. Badger*, 6 Hun, 293 (1875); *aff'd*, 67 N. Y. 294; *Whitehall & P. R. R. Co. v. Myers*, 16 Abb. Pr. (N. S.) 34 (1872). But see *Brewers Fire Ins. Co. v. Burger*, 10 Hun, 56 (1877), holding that where the original subscription contract is verbal and complete, and a part only of it is afterwards reduced to writing, it is competent to prove the whole agreement. See also *Hendrix v. Academy of Music*, Georgia, 1885. *Cf. Eighmie v. Taylor*, 98 N. Y. 288 (1885).

In Georgia, under § 3,803 of the Code, where the subscription does not purport to contain the whole contract, parol evidence

is admissible. *Hendrix v. Academy of Music*, 73 Ga. 437 (1884).

In Pennsylvania, the case *McClure v. People's Freight Ry. Co.*, 90 Pa. St. 269 (1879), sustains the general rule, and excluded a parol agreement or condition allowing payment in property. But *Rinesmith v. People's Freight Ry. Co.*, 90 Pa. St. 262 (1879); *Caley v. Phil. & Chester R. R. Co.*, 80 Penn. St. 363 (1876); *Miller v. Hanover Junc. & Sus. R. R. Co.*, 87 Penn. St. 95 (1878); and *McCarty v. Selinsgrove & N. B. R. R. Co.*, 87 Penn. St. 332 (1878), allow parol evidence to contradict the subscription contract where it is shown that but for the parol agreement the subscription would not have been made, the last two cases saying, however, that the evidence is inadmissible if other stockholders are interested in opposition to such parol agreement. This unusual rule probably has its origin in an old English case (*Pulsford v. Richards*, 17 Beav. 87, 1853) which holds that a representation is to be considered *fraudulent* when, "if the real truth had been stated, it is reasonable to believe the plaintiff would not have entered into the contract."

The subscriber's remedy is against the person who made the agreement which has not been kept. *Felgate's Case*, 2 De G., J. & S. 456 (1865). An action for damages for breach of contract lies against the corporation if the agreement amounts to a condition subsequent.

ment, applies to a subscription contract for stock in a corporation. Neither party is permitted to prove a different contract from that expressed in the written instrument. Under the rule, not even a separate written cotemporaneous contract is admissible to change the subscription contract.¹

§ 138. Thus an agreement that a certain location will be adopted,² or that payment may be made in a certain way or at a certain time,³ or that the subscription shall be merely nominal for the purpose of inducing others to subscribe,⁴ or that the subscription shall be, in fact, only a pledge of stock by the corporation to the subscriber, or that the stock may be surrendered,⁵ or that certain property would be purchased by the corporation,⁶ or that the subscriber might keep his stock, but should not be liable for the full par value thereof,⁷ or that payment would not be demand-

¹ *Brownlee v. O. Ind. & Ill. R. R. Co.*, 18 Ind. 68 (1862); *White Mts. R. R. Co. v. Eastman*, 34 N. H. 124 (1856).

² *North Car. R. R. Co. v. Leach*, 4 Jones' Law (N. C.), 340 (1857); *Wight v. Shelby R. R. Co.*, 16 B. Monr. 4 (1855); *Ellison v. Mobile & O. R. R. Co.*, 36 Miss. 572 (1858); *Miss. O. & R. R. Co. v. Cross*, 20 Ark. 443 (1859); *Killer v. Johnson*, 11 Ind. 337 (1858); *Evansville, Indianapolis, & C. S. R. R. Co. v. Posey*, 12 Ind. 363 (1859); *Eakright v. Logansport & N. Ind. R. R. Co.*, 13 Ind. 404 (1859); *Carlisle v. Evansville, Ind., & C. S. R. R. Co.*, 13 Ind. 477 (1859); *Miller v. Wild Cat Gravel Road Co.*, 52 Ind. 51 (1875); s. c., 57 Id. 241; *Miller v. Hanover Junc. & Sus. R. R. Co.*, 87 Pa. St. 95 (1878); *Gelpcke v. Blake*, 15 Iowa, 387 (1863); *Braddock v. Phil., M. & M. R. R. Co.*, 45 N. J. Law Rep. 363 (1883); *Killer v. Johnson*, 11 Ind. 337 (1858), holding it immaterial that fraud was actually intended. *Contra*, *Rives v. Montgomery S. P. R. Co.*, 30 Ala. 92 (1857).

³ *Noble v. Collender*, 20 O. St. 199 (1870); *Henry v. Vermilion & A. R. R. Co.*, 17 O. 187 (1848); *Stewards of M. E. Church v. Town*, 49 Vt. 29 (1876); *Ridgefield & N. Y. R. R. Co. v. Brush*, 43 Conn. 86 (1875); *Thigpen v. Miss. Central R. R. Co.*, 32 Miss. 347 (1856).

⁴ *Downie v. White*, 12 Wis. 176 (1860). *Wetherbee v. Baker*, 35 N. J. Eq. 501 (1882); *Kishacoquillas & Centre T. R. Co. v. McCanahy*, 16 S. & R. (Pa.) 140 (1827); *Phoenix W. Co. v. Badger*, 6 Hun, 293 (1875); *aff'd*, 67 N. Y. 294; *Psychaud*

v. Hood 23 La. Ann. 732 (1871); *Cleveland Iron Co. v. Ennor*, 12 Am. & Eng. Corp. Cases 88 (Ill., 1886); *Robinson v. Pittsburgh & C. R. R. Co.*, 32 Pa. St. 334 (1858); *Graff v. Pittsburgh & S. R. R. Co.*, 31 Pa. St. 489 (1858); *Mann v. Cooke*, 20 Conn. 178 (1849); *Conn. & Pass. Rivers R. R. v. Bailey*, 24 Vt. 465; *Davidson's Case*, 3 De G. & S. 21 (1849), holding it to be a fraud on other subscribers, without requiring proof that there were such. *Bridger's Case*, L. R. 9 Eq. Cas. 74 (1869); *New Albany & Salem R. R. Co. v. Slaughter*, 10 Ind. 218 (1858); *Blodgett v. Morrill*, 20 Vt. 509 (1848); *Minor v. Mechanics Bk. of Alexandria*, 1 Peters, 46 (1828); *Bates v. Lewis*, 3 O. St. 459 (1854); *Litchfield Bk. v. Church*, 29 Conn. 137 (1860); *Mangles v. Grand Collier Dock Co.*, 10 Sim. 519 (1840); *Preston v. Grand Collier Dock Co.*, 2 Rail. Cas. 335 (1840); *Chouteau Co. v. Floyd*, 74 Mo. 286 (1881). These cases hold that such agreements are void as a fraud on corporate creditors and on other subscribers, and that the subscription is enforceable absolutely.

⁵ *Melvin v. Lamar Ins. Co.*, 80 Ill. 446 (1875); *White Mts. R. R. Co. v. Eastman*, 34 N. H. 124 (1856). Or that the subscriber be released. *Gill v. Balis*, 72 Mo. 424 (1880).

⁶ *Kelsey v. Northern Light Oil Co.*, 45 N. Y. 505 (1871).

⁷ *Custar v. Titusville Gas & Water Co.*, 63 Pa. St. 381 (1869); *Union Ins. Co. v. Frear S. Mfg. Co.*, 97 Ill. 537 (1881); *Upton v. Tribilcock*, 91 U. S. 45 (1875).

ed until certain work had been completed,¹ or that the money would be applied to a particular part of the road,² or other similar executory contracts are held to be no defense to an action to collect the subscription.³ Where, for the purpose of obtaining a subscription, a promise was made in behalf of the corporation that a branch road would be built, it was held that this promise was but an expression of an existing intention which was liable to be changed, and was no defense.⁴ It is also held that a promise which, if carried out, would necessitate an *ultra vires* act by the corporation, is not binding, and is no defense.⁵

§ 139. *Corporation chargeable with the fraudulent representations of their agents.*—At an early day in England it was held in a number of cases that corporations were not bound by the frauds of their agents in obtaining subscriptions to stock.⁶ This doctrine rested on the theory that the corporation gave the agent no power or authority to commit a fraud, and that, consequently, the fraud rendered the agent liable personally, but did not release or affect the subscription.

§ 140. The modern doctrine, however, both in this country and in England, has completely exploded the theory that corporations are not chargeable with the frauds of their agents in taking subscriptions. The well established rule now is that a corporation cannot claim or retain the benefit of a subscription which has been

¹ *La Grange & M. P. R. Co. v. Mays*, 29 Mo. 64 (1859); *Clem v. Newcastle & D. R. R. Co.*, 9 Ind. 488 (1857), holding that such a promise is contradictory of the legal effect of the subscription. *Cincinnati U. & Ft. Wayne R. R. Co. v. Pearce*, 28 Ind. 502 (1867).

² *Smith v. Tallahassee Branch of C. P. R. Co.*, 30 Ala. 650 (1857).

³ *Piscataqua Ferry Co. v. Jones*, 39 N. H. 491 (1859); *Crossman v. Penrose Ferry Bridge Co.*, 26 Pa. St. 69 (1856); *New Albany & Salem R. R. Co. v. Fields*, 10 Ind. 187 (1858); *East Tenn. & Va. R. R. Co. v. Gammon*, 5 Sneed. (Tenn.) 567 (1858); *Saffold v. Barnes*, 39 Miss. 399 (1860); *Payson v. Withers*, 5 Biss. 269 (1873); *Goff v. Hawkeye Pump & W. M. Co.*, 62 Iowa, 691 (1884); *Corwith v. Culver*, 69 Ill. 502 (1873). *Contra*, *Mahan v. Wood*, 44 Cal. 462 (1872), where the par value of the shares were not what was promised.

⁴ *McAllister v. Indianapolis & Cin. R. Co.*, 15 Ind. 11 (1860).

⁵ *Johnson v. Crawfordsville, F. K. & Ft. W. R. R. Co.*, 11 Ind. 280 (1858), where aid from another railroad was promised. *Peters v. Lincoln & N. W. R. Co.*, 14 Fed. Rep. 319 (1882), where an *ultra vires* lease was promised. *Baile v. Calvert C. E. Soc.*, 47 Md. 117 (1877).

⁶ *Dodgson's Case*, 3 De G. & Sm. 85 (1849); *Bernard's Case*, 5 De G. & Sm. 283 (1852); *Gibson's Case*, 2 De G. & J. 275 (1858); *Holt's Case*, 22 Beav. 48 (1856); *Felgate's Case*, 2 De G., J. & S. 456 (1865); *Mixer's Case*, 4 De G. & J. 575, where a prospectus was issued by the directors; *Ayres' Case*, 25 Beav. 513 (1858), the court holding that the corporation is bound by the misrepresentation only where it expressly authorized the particular statement made. *Cf. Barry v. Craskey*, 2 Johns. & Hem. 1 (1861).

obtained through the fraud of its agents. The misrepresentations are not regarded as having actually been made by the corporation, but the corporation is not allowed to retain the benefit of the contract growing out of them, but is liable to the extent that it has profited by such misrepresentations.¹ The question of the authority of the agent taking the subscription is immaterial herein. It matters not whether he had any authority, or exceeded his authority, or concealed its limitations.² The corporation cannot claim the benefits of his fraud without assuming also the representations which procured those benefits. Parol evidence is admissible to show the fraud, since it does not vary or contradict the contract, but shows that no contract was properly formed.³

§ 141. *The misrepresentations must be by authorized agents.*

—False representations by persons who do not act as intermediaries between the corporation and the subscriber in forming the contract cannot bind the corporation nor affect the subscription. They are statements of outside parties.⁴ The subscriber may have his action for damages against such persons for deceit, but he cannot charge the corporation with their misrepresentations. Sometimes, also, the misrepresentations even of persons connected with the corporation do not bind the corporation, inasmuch as their powers are purely statutory or have nothing to do with the taking of subscriptions. Thus, while there has been considerable controversy in this country over the question of fraudulent representa-

¹ *Western Bk. of Scotland v. Addie, L. R. 1 Sc. App. Cas. 145*; *Natl. Exchange Co. v. Drew, 32 Eng. L. & Eq. 1* (1853); *Henderson v. Lacon, L. R. 5 Eq. Cas. 249* (1867); *Ex parte Linger, 5 Irish Ch. Rep. N. S. 174*; *Montgomery S. Ry. Co. v. Matthews, 77 Ala. 357* (1884). The principles governing these contracts are the same as the principles governing contracts between private individuals. *Directors, &c., of Central Ry. v. Kisch, L. R. 2 H. L. App. Cas. 99* (1870); *Anderson v. Newcastle & Richmond R. R. Co., 12 Ind. 376* (1859); *Vreeland v. N. J. Stone Co., 29 N. J. Eq. 188* (1878).

² *Crumbe v. U. S. Min. Co., 7 Gratt. (Va.), 353* (1851). Provided, of course, that the misrepresentations were made by persons legally connected with the taking of the subscription. An agent to obtain subscriptions may use the ordinary means of accomplishing the object of his appointment, such as representing the loca-

tion and quality of the lands and the like. *Sandford v. Handy, 23 Wend. 260* (1840). See also *Nelson v. Cowing, 6 Hill, 336* (1844).

³ *N. Y. Exchange Co. v. De Wolf, 31 N. Y. 271* (1865); *Jewett v. Valley Ry. Co., 34 O. St. 601* (1878). In Pennsylvania the peculiar rule prevails that the agent's misrepresentations affect the subscription and are a defense only when the agent actually had or reasonably appeared to have authority to make representations. This was the ancient English doctrine, long since abandoned. *Custar v. Titusville Gas & Water Co., 63 Pa. St. 381* (1869).

⁴ *Cunningham v. Edgefield & Ky. R. R. Co., 2 Head, 23* (1858). The representations made to him by other subscribers or outsiders are immaterial herein. His remedy is against them personally. *Duranty's Case, 26 Beav. 268* (1858); *Ex parte Frowd, 30 L. J. (Ch.), 322* (1860).

tions by commissioners having statutory powers to take subscriptions, it is quite well settled that the subscriber is bound to know that the commissioners have no power to make representations, and that the corporation is not bound thereby.¹ So also it has been held that the representations by the president of the corporation do not bind it where he had no authority to take subscriptions.² In Indiana it is held that an agent taking subscriptions before the incorporation of the company cannot bind it by his misrepresentations.³ If there is conflicting testimony as to the authority and *status* of the agent, the question is to be submitted to the jury.⁴

§ 142. *Corporation not bound by misrepresentations of officers at a public meeting.*—There is a difference of opinion among the authorities as to whether fraudulent representations made by one or more of the company's officers, at a public meeting, called to promote the procuring of subscriptions, are chargeable against the corporation where such representations were not expressly authorized by the corporation. In New York, Iowa, Alabama and Louisiana, such misrepresentations do not bind the corporation.⁵ In Georgia and Wisconsin, on the other hand, such fraudulent representations are held to be admissible in evidence.⁶ The former rule seems to accord most with the modern tendency of the decisions, which go very far towards the enforcement of subscriptions, after corporate creditors and other subscribers have become interested in the enterprise.

¹ *Nippanose Mfg. Co. v. Staddon*, 68 Pa. St. 256 (1871); *Barrington v. Pittsburgh & Steubenville R. R. Co.*, 34 Pa. St. 358 (1859); *Wight v. Shelby R. R. Co.*, 16 B. Monr. 4 (1855); *Rutz v. Esler & R. Mfg. Co.*, 3 Bradw. 81 (1878); *Syracuse, P. & O. R. R. Co. v. Gere*, 4 Hun, 392 (1875); *North Car. R. R. Co. v. Leach*, 4 Jones' L. (N. C.) 340 (1857).

² *Crump v. U. S. Mining Co.*, 7 Gratt. (Va.) 353 (1851); *Rives v. Montgomery South Plank R. Co.*, 30 Ala. 92 (1857). In all such cases, however, if the corporation accepts a subscription taken by an unauthorized agent, it cannot retain the subscription and repudiate the representations. It must assume both or neither.

³ *Miller v. Wild Cat Gravel Road Co.*, 57 Ind. 241 (1875).

⁴ *Kelsey v. Northern Light Oil Co.*, 45 N. Y. 505 (1871); *Crump v. U. S. Mining Co.*, 7 Gratt. (Va.) 353 (1851).

⁵ *Buffalo & N. Y. City R. R. Co. v. Dudley*, 14 N. Y. 336 (1856); *First Natl. Bk. v. Hurford*, 29 Iowa, 579 (1870); *Smith v. Tallahassee Branch of C. P. R. R. Co.*, 30 Ala. 650 (1857), on the ground of a want of authority which the subscriber is bound to know; *Vicksburg, S. & T. R. R. v. McKean*, 12 La. Ann. 638 (1857), on the ground that if the rule were otherwise, "there will be very little security to those who loan money or render assistance to institutions of this kind."

⁶ *Atlanta & West Point R. R. Co. v. Hodnett*, 36 Ga. 669 (1867); *McClellan v. Scott*, 24 Wis. 81 (1869).

§ 143. *The misrepresentations may arise by prospectuses.*—

A prospectus issued by the authority of the directors or the stockholders of a corporation, may be relied upon by a person in subscribing for stock, and if the prospectus contains a false representation, and the subscription is made by reason thereof, such representation is binding upon the corporation.¹ In this class of corporate instruments, however, it is held, that some high coloring and even exaggeration is allowable. "In an advertisement of this description, some allowance must always be made for the sanguine expectations of the promoters of the adventure, and no prudent man will accept the prospects which are always held out by the originators of every new scheme, without considerable abatement."² So, also, if the language used in the prospectus admits of two meanings, the subscriber, relying on it, must ascertain which meaning is intended.³ Unless the representation distinctly refers to what is actually existing at the time, it must be taken to represent what will result when the enterprise is carried out, and will then be merely an expression of opinion.

§ 144. *Or by reports.*—So, also, a report, made by the corporate officers to the stockholders, may be relied on by one who contemplates subscribing for stock.⁴ The corporation cannot say

¹ *Oakes v. Turquand*, L. R., 2 H. L. App. Cas. 325 (1867); *Ross v. Estates Investment Co.*, L. R., 3 Ch. App. 682 (1868); *Reese River Silver Min. Co. v. Smith*, L. R., 4 H. L. 64 (1869); *Blake's Case*, 34 Beav. 639 (1865); *Henderson v. Lacon*, L. R. 5 Eq. Cas. 249 (1867). In England, it is enacted by sect. 38 of the Companies Act, 1867, "Every prospectus of a company, and every notice inviting persons to subscribe for shares in any joint-stock company, shall specify the dates and names of the parties to any contract entered into by the company, or the promoters, directors, or trustees thereof, before the issue of such prospectus or notice, whether subject to adoption by the directors or the company or otherwise; and any prospectus or notice not specifying the same, shall be deemed fraudulent on the part of the promoters, directors, and officers of the company knowingly issuing the same, as regards any person taking shares in the company on the faith of such prospectus, unless he shall have had notice of such contract." For the application of this statute see *Cornell v. Hay*, 8 C. P. 328 (1873); *Gover's Case*, L.

R., 20 Eq. 114 (1875); *Davidson v. Tulloch*, 1 MacQ. 783; *Arkright v. Newbold*, L. R., 17 Ch. D. 311 (1880); *Twy-cross v. Grant*, L. R., 2 C. P. D. 469 (1877); *Emma Min. Co. v. Lewis*, L. R., 4 C. P. D. 396 (1879); *Bagnall v. Carlton*, L. R., 6 Ch. D. 371 (1877); *Plympton Min. Co. v. Wilkins*, 1882, W. N. p. 66; *Sullivan v. Metcalfe*, L. R., 5 C. P. Div. 455 (1880). For other cases see *Hurrell v. Hyde on Joint Stock Companies* (1883) 25.

² *Directors, &c. of Central Ry. Co. v. Kisch*, L. R., 2 H. L. App. Cas. 99 (1870).

³ *Smith v. Chadwick*, L. R., 9 H. L. 187; *Hallows v. Fermie*, L. R., 3 Ch. App. 467 (1868), where the court says, "If they may be construed in a different manner by different minds, it will be impossible to test the truth of any one man's assertion, that he understood them in the sense in which they involved a misrepresentation." See also Ch. XX.

⁴ *Western Bk. of Scotland v. Addie*, L. R., 1 Sc. App. Cas. 145; *New Brunswick & C. Ry. Co. v. Conybeare*, 9 H. L. Cas. 711 (1862).

that such reports were intended for the stockholders alone. The law holds that the report is known, and is intended to be known to all persons who contemplate becoming stockholders, and is the same as though published to the world.¹

§ 145. *Misrepresentations amounting to fraudulent representations.*—Any statement, by the authorized agents of a corporation, in regard to the past or present *status* of the corporate enterprise or material matters connected therewith, whereby subscriptions are obtained, is a fraudulent representation.

Thus, a false statement that a certain amount of stock had been subscribed for;² or that certain property had been purchased;³ that the corporate property is unincumbered;⁴ that the corporation is solvent and prosperous;⁵ that the directors have subscribed for stock;⁶ that certain individuals are directors;⁷ or as to the nature of the business to be undertaken;⁸ or in England, where the memoranda or articles of the association are different from the prospectus;⁹ or that work on the enterprise had reached a certain stage of completion;¹⁰ or that the

¹ Natl. Exchange Co. v. Drew, 32 Eng. L. & Eq. 1 (1855); Scott v. Dixon, 29 L. J. (Ex.), 62, n.; explained and adopted in L. R., 6 H. L., 377.

² Ross v. Estates Investment Co., L. R., 3 Ch. 682 (1868); Henderson v. Lacon, L. R., 5 Eq. 249 (1867).

³ Also that the property contained valuable mines, in full operation, and with large daily returns. Reese River Silver Min. Co. v. Smith, L. R., 4 H. L. 64 (1869); Waldo v. Chicago, St. P. & F. D. L. R. R. Co., 14 Wis. 575 (1861); Ross v. Estates Investment Co., *supra*. Representation that a certain patent right owned by the company had been tested, and found to be valuable, held not a misrepresentation, although it turns out to be worthless. Denton v. Macneil, L. R., 2 Eq. 352 (1866). Representation in good faith, that title to land was good when in fact it was bad, is not a misrepresentation. New Brunswick & C. Ry. Co. v. Conybeare, 9 H. L. Cas. 711 (1862). But misrepresentation that a government guarantee had been obtained is material. Kisch v. Central Ry. of Venezuela, 34 L. J. (Ch.) 545.

⁴ McClellan v. Scott, 24 Wis. 81 (1869); Water Valley Mfg. Co. v. Seaman, 58 Miss. 655.

⁵ Bell's Case, 22 Beav. 35 (1856);

Melendy v. Keen, 89 Ill. 395 (1878); Western Bk. of Scotland v. Addie, L. R., 1 Sc. App. Cas. 145. Not so, however, where the directors honestly figured in debts which afterwards turned out to be bad. Jackson v. Turquand, L. R., 4 H. L. 305 (1869).

⁶ Henderson v. Lacon, L. R., 5 Eq. Cas. 249 (1867).

⁷ Blake's Case, 34 Beav. 639 (1865); Munster's Case, 14 W. R. 957 (1866). Persons who have accepted are directors, although without the qualification shares. Hallows v. Fernie, L. R., 3 Ch. App. 467 (1868).

⁸ Blackburns' Case, 3 Drew. 409 (1856).

⁹ Downes v. Ship, L. R., 3 H. L. 343 (1868); Briggs, L. R., 1 Eq. Cas. 483 (1866).

¹⁰ Peel's Case, L. R., 2 Ch. App. 674 (1867); Ogilvie v. Currie, 37 L. J. (Ch.) 541 (1868); Lawrence's Case, L. R., 2 Ch. App. 412 (1867); Kincaid's Case, Id. (1867); Wilkinson's Case, L. R., 2 Ch. App. 536 (1867); Ashley's Case, L. R., 9 Eq. Cas. 263 (1870); Stewart's Case, L. R., 1 Ch. App. 574; Whitehouse's Case, L. R., 3 Eq. 790 (1867); Taite's Case, L. R., 3 Eq. 795 (1867); Upton v. Hansbraugh, 3 Biss. 417 (1873); Re Cachar Co., 36 L. J. (Ch.) 490 (1867); Ship v.

objects of the enterprise set forth in the subscription contract were of a certain nature, the subscriber not reading or hearing, and not being able to read the contract,¹ have been held to constitute a fraudulent representation, entitling the subscriber induced thereby to subscribe, to the remedies provided by law for such cases. In all these cases, however, the distinction between statements relative to the prospects and capabilities of the enterprise, and statements specifically specifying what does or does not exist, must be carefully borne in mind. The former are matters of opinion; the latter are material representations and are fraudulent if false.²

§ 146. *Statements as to questions of law.*—Where a subscription is obtained by a false representation as to the legal effect of the subscription contract, or of corporate rights or liabilities, the subscriber has no remedy. He is bound to take notice of the law.³ Thus a misrepresentation as to the extent to which the subscriber would be liable on his stock,⁴ or that he may allow his stock to be forfeited,⁵ or that payment would not be demanded until the enterprise was partly or wholly completed,⁶ is a statement as to the law. It states that something can be done, which the law prohibits from being done.

Cresskill, L. R., 10 Eq. Cas. 73 (1870). Cf. *Ex parte Briggs*, L. R., 1 Eq. Cas. 483 (1866); *Stewart's Case*, L. R., 1 Ch. 574 (1866).

¹ *West v. Crawfordsville & A. T. Co.*, 19 Ind. 242 (1862).

² Whether the statement refers to a "possibility or a contingency, or an intention," or to an existing fact, is a question sometimes for the jury, sometimes for the judge, generally the latter. *Edgington v. Fitzmaurice*, L. R., 29 Ch. D. 459 (1885). All the statements, together with the circumstances and history of the matter, are to be considered in deciding whether a misrepresentation was made. It is sufficient if the subscriber replied partly on the misrepresentation. He need not have relied on it exclusively. *Id.* See also *Nicol's Case*, 3 De G. & J. 420 (1858). The subscriber may, by contract, waive his right to rely on a representation. *Brownlee v. Campbell*, L. R., 5 App. Cas. 925 (1880). In the case *Montgomery S. Ry. Co. v. Matthews*, 77 Ala. 357 (1884), the court said: "An opinion expressed, even if not realized,

cannot, without more, become a fraudulent representation. If, however, such opinion is falsely expressed, with intent to deceive, and does deceive, this constitutes such opinion or representation a false statement of fact, and vitiates a contract thereby procured, unless the representation relates to a matter equally open to both parties." Although the misrepresentation was innocently made, yet it may suffice to avoid the subscription.

³ *Parker v. Thomas*, 19 Ind. 213 (1862).

⁴ *Upton v. Tribilcock*, 91 U. S. 45 (1875), where the representation was that only a certain percentage could be called for. In *Upton v. Englehart*, 3 Dill. 496 (1874), this representation was held to be a defense, where it was made in one State with reference to the laws of another State. See also *Accidental Ins. Co. v. Davis*, 15 L. T. 182 (1866), where it was represented that further calls were not contemplated.

⁵ *N. E. R. R. Co. v. Rodrigues*, 10 Rich. (S. C.) 278 (1857).

⁶ *Clem v. Newcastle & Danville R. R. Co.*, 9 Ind. 488 (1857).

§ 147. *Misrepresentation may be by suppression of the truth.*

—The misrepresentation, entitling the subscriber to his remedies, may consist in the suppression of what is true, as well as in the assertion of what is false.¹ Where any statement is made at all, it must be a fair and full statement of all the material facts. The corporate authorities, in issuing a prospectus, are “bound to state everything with strict and scrupulous accuracy, and not only to abstain from stating as fact, that which is not so, but to omit no one fact within their knowledge, the existence of which might, in any degree, affect the nature, or extent, or quality of the privileges and advantages which the prospectus holds out as inducements to take shares.”² Thus, an omission to state that a very large sum had been paid for property, the merits of which were fully set forth, has been held to be equivalent to a fraudulent representation.³ On the other hand, a failure to state that large sums were paid to the directors to induce them to act as such, was held not to be a fraudulent omission.⁴

§ 148. *Misrepresentation may be by statements made without knowledge of their falsity.*—Statements need not be intentionally false, in order to amount to a fraudulent representation.⁵ A

¹ “No misstatement or concealment of any material facts or circumstances ought to be permitted. . . . The suppression of a fact will often amount to a misrepresentation.” *Directors, &c., of Central Ry. v. Kisch*, L. R., 2 H. L. App. Cas. 99 (1867). In *Oakes v. Turquand*, L. R., 2 H. L. App. Cas. 325 (1867), the court says the prospectus is objectionable, “not that it does not state the truth as far as it goes, but that it conceals most material facts with which the public ought to have been made acquainted, the very concealment of which gives to the truth which is told the character of falsehood.”

² *New Brunswick & Con. Ry. Co. v. Muggeridge*, 1 Dr. & Sm. 363, 381 (1860).

³ *Directors, &c., of Central Ry. Co. v. Kisch*, *supra*. In *Gover's Case*, L. R., 1 Ch. D. 182 (1875), under different circumstances, the contrary was held.

⁴ *Heymann v. European Central Ry. Co.*, L. R., 7 Eq. Cas. 154 (1868). Statement need not be made that stock had been given to the directors and promoters in payment for services. *Pulsford v. Richards*, 17 Beav. 87 (1853). Nor as to the amount of stock already subscribed. *Vane v. Cobbold*, 1 Ex. 798 (1848).

⁵ Corporate agents, making representations in order to obtain subscriptions, are bound to know the truth or falsity of such statements. *Reese River Co. v. Smith*, L. R., 4 H. L. 64 (1869); aff'g L. R., 2 Eq. 264; *Glamorganshire Iron, &c., Co. v. Irvine*, 4 F. & F. 947 (1866), applying the same rule at law. The English case of *Kennedy v. Panama, N. J. & A. R. M. Co.* (L. R., 2 Q. B. 580) (1867), holds, however, that “where there has been an innocent misrepresentation or misapprehension, it does not authorize a rescission, unless it is such as to show that there is a complete difference in substance between what was supposed to be and what was taken, so as to constitute a failure of consideration,” and that to hold otherwise would be to make a warranty out of the representation. In the recent case, *Edgington v. Fitzmaurice*, L. R., 29 Ch. D. 459 (1885), the court says that a statement of fact, which the person making does not know the truth of, is “in the eye of the law, a fraudulent statement as much as if the parties making it had known it to be false.” In this country, the cases seem to favor a different rule. The party making the representations

false statement, made in good faith, but in ignorance, is, in a legal point of view, the same as an assertion which the party knew to be untrue.¹ Thus, a prospectus issued by the directors, representing the corporate property as containing valuable mines, all of which was in good faith, but false, is the same as though the statements were made with knowledge of their falsity. Where, however, the statement in good faith was that the corporation had a government contract, which, upon litigation, was found to be untrue, the representation was held not to be fraudulent.²

§ 149. *Misrepresentations that are insufficient.*—It is not every misrepresentation that enables a subscriber to set up that he was induced to subscribe by fraud.³ Thus an honest mistake of judgment, on the part of the directors, as to the collectibility of certain debts, whereby a company represented to be solvent turns out to be insolvent, is not a fraudulent representation. So, also, of a representation as to the value of a patent right, which, it was stated, would be tested further. On the other hand, a statement made with the intent to defraud the subscriber, but without that effect, is immaterial; mere intent without damage is insufficient.⁴ A misstatement as to the contents of the subscription contract, which the subscriber signs, is immaterial, where he can read, but does not.⁵ And where false representations are made, but before the subscription is completed, the representations are made good

must be proven "to have had a fraudulent purpose in contemplation, or at least to have known that the statements were untrue." *Nugent v. Cin., Harrison & Indianapolis S. L. R. R. Co.*, 2 Disney, 302; *Selma, M. & M. R. R. Co. v. Anderson*, 51 Miss. 829 (1876); *Cunningham v. Edgefield & Ky. R. R. Co.*, 2 Head, 23 (1858). See also *Chitty on Contracts*, 682. The vigorous case of *Henderson v. R. R. Co.*, 17 Tex. 560 (1856), however, effectively sustains the opposite view. See also 1 *Story Eq. Juris*, § 193; *Story on Agency*, §§ 127, 135, 137, 452.

¹ *Reese River Co. v. Smith, L. R.*, 4 H. L. 64 (1869).

² *Kennedy v. Panama, N. Z. & O. R. M. Co.*, L. R., 2 Q. B. 580 (1867).

³ Mere matters of opinion, as to whether the enterprise can be completed, or when it will be completed, or the prospects of profits, cannot be misrepresentations. The subscriber is bound to

know that these are all matters of mere conjecture. *Brownlee v. O. Ind. & Ill. R. R. Co.*, 18 Ind. 68 (1862); *Pickering v. Templeton*, 2 Mo. App. 424 (1876); *Hughes v. Antietam Mfg. Co.*, 34 Md. 316 (1870); *Hardy v. Merriweather*, 14 Ind. 203 (1860); *Andrews v. O. & Miss. R. R. Co.*, 14 Ind. 169 (1860); *Bish v. Bradford*, 17 Ind. 490 (1861); *Walker v. Mobile R. R. Co.*, 34 Miss. 245 (1857); *Coil v. Pittsburgh College*, 40 Penn. St. 439 (1861). See also § 92. In the cases, however, of *Gerhard v. Bates*, 17 Jur. 1097 (1853), and *Taylor v. Ashton*, 11 M. & W. 401 (1843), it was held that a false guarantee of the promoters, that a certain dividend would result from the enterprise, constituted a false representation.

⁴ *Killer v. Johnson*, 11 Ind. 337 (1858); *Cunningham v. Edgefield & Ky. R. R. Co.*, 2 Head, 23 (1858).

⁵ *Thornburgh v. Newcastle & Danville R. R. Co.*, 14 Ind. 499 (1860).

by intervening events, the subscribers cannot complain.¹ Frauds of the directors which are not the subject of a representation, are not to be remedied by the principle of law governing the subject of false representation.²

§ 150. *Subscriber is not bound to investigate the truth of representations.*—If a subscriber has used reasonable caution and judgment in accepting the statements of corporate agents, it is no answer to his claim, that he was induced to subscribe by fraudulent representations, to say that by proper inquiry he might have learned the truth, or by more vigilance he might have discovered the deception.³ Where the representations are by a prospectus, he is not obliged to examine documents referred to, even though such examination would have shown the falsity of the representations.⁴ In New York, the general principle of law governing cases of misrepresentation is clearly stated to be that “every contracting person has an absolute right to rely on the express statement of an existing fact, the truth of which is known to the opposite party, and unknown to him, as a basis of a mutual engagement, and he is under no obligation to investigate and verify statements, to the truth of which the other party to the contract, with full means of knowledge, has deliberately pledged his faith.”⁵ It is not incumbent upon him to institute inquiries, and to suspect fraud when all seems fair. But where the means of information are open equally to both parties, the subscriber has no right to rely upon the representations of the corporate agent, unless the latter dissuades the subscriber from investigation.⁶ So also where the subscriber reads several documents, he cannot rely on representations in one which are corrected and limited by statements in the others, even though he claims to have overlooked such corrections.⁷

¹ *Ship v. Cresskill*, L. R., 10 Eq. Cas. 73 (1870).

² *Hornaday v. Ind. & Ill. Central R. R.*, 9 Ind. 263 (1857); *Heymann v. European Central Ry. Co.*, L. R., 7 Eq. Cas. 154 (1868).

³ *New Brunswick & Can. Ry. Co. v. Muggeridge*, 1 Dr. & Sm. 363; *Upton v. Englehart*, 3 Dill. 496 (1874); *Directors, &c., of Central Ry. v. Kisch*, L. R., 2 H. L. App. Cas. 99 (1870). *Cf. Hallows v. Firmie*, L. R., 3 Ch. App. 467 (1868). The subscriber is not bound to investigate

the truth of statements which the other party with full knowledge of the facts makes. *McClellan v. Scott*, 24 Wis. 81 (1869).

⁴ *Kisch v. Central Ry.*, 34 L. J. (Ch.) 545; s. c. *supra*.

⁵ *Mead v. Bunn*, 32 N. Y. 274 (1865).

⁶ *Jennings v. Braughton*, 22 L. J. (Ch.) 583 (1853); *Walker v. Mobile & O. R. R. Co.*, 34 Miss. 245 (1857).

⁷ *Scholey v. Central Ry. Co.*, L. R., 9 Eq. Cas. 766, n. (1870).

§ 151. *Subscriptions induced by fraudulent representations are not void, but only voidable.*—The principle of law, that fraud vitiates all contracts, applies to a contract of subscription, but this principle means, not that the contract is void *per se*, from the formation of the contract, but that the contract is voidable at the option or election of the person defrauded.¹ Until such election is exercised, the contract is enforceable by both or either of the parties. Hence a subscription to stock, obtained by fraudulent representations, is not void from the time when it was made, nor is it void until it is ratified and confirmed by the defrauded subscriber, but it is valid until it is expressly rescinded and repudiated by the subscriber.² This principle is important in determining the method of rescission, and particularly the time within which a rescission must be made.

§ 152. *Remedies of a subscriber induced to subscribe by fraudulent representations.*—There are, in general, five different remedies which are open to a subscriber induced to subscribe by fraud. He may, upon discovering the fraud, rescind the subscription by notification to the corporate authorities, without taking legal proceedings; or he may wait until sued upon the subscription, and then set up the fraud as a defense to the action at law; or he may file a bill in equity to restrain such suits at law, and to set aside the subscription contract, and also, if he wishes, to recover back payments already made on the subscription; or he may bring an action at law against the parties fraudulently inducing the subscription, and recover damages for the deceit; or he may sue for money had and received.

§ 153. *Rescission without legal proceedings.*—It is the duty and the right of directors, without waiting for a bill in equity or other legal proceedings, to revoke a subscription contract, and remove from the stockholders' list the name of a subscriber who reasonably proves that he was induced to subscribe by fraudulent representations, chargeable to the corporation, and who requests a rescission of the subscription.³ The directors are not bound to

¹ *Oakes v. Turquand*, L. R., 2 H. L. App. Cas. 325 (1867); *Upton v. Englehart*, 3 Dill. 496 (1874); *Reese River Min. Co. v. Smith*, L. R., 4 H. L. 64 (1869).

² *Tennant v. City of Glasgow Bk.*, L. R., 4 App. Cas. 615.

³ *Wright's Case*, L. R. 2 Eq. 331; s. o. L. R. 7 Ch. 55 (1871); *Blake's Case*, 34 Beav. 639 (1865); *Reese River Co. v. Smith*, L.

make a hopeless defense. It is an ordinary business act within the powers of the directors, and their discretion is not to be controlled unless unreasonably exercised. Where, however, upon such a demand being made by the subscriber, the directors refuse to dissolve the subscription contract, the subscriber must resort to a bill in equity to have the contract set aside for fraud.¹ A mere notification to the corporation is insufficient.

§ 154. *False representation as a defense to an action at law for calls.*—The most common remedy of a subscriber induced by fraud to subscribe is to wait until the corporation brings suit to collect the subscriptions, and then to set up the fraud as a defense. Nearly all of the cases in this country are cases where this remedy has been adopted.² It is subject, however, to the danger that the corporation may become insolvent, and thereby bar the defense. The decided tendency of the law to preserve the rights of third persons will probably and properly tend to defeat this defense in all cases where the subscriber has not filed a bill in equity promptly upon discovering the fraud, instead of waiting to be sued by the corporation. The intervening rights of stockholders and corporate creditors call for prompt action on the part of a subscriber who seeks to avoid his liability because of fraud.

§ 155. *Remedy by bill in equity.*—This is the most fair, safe, and complete remedy that the subscriber has. It is a decisive notice to the corporation and all third parties not to rely upon the subscription in question. It avoids the risk of future corporate insolvency. It enables the subscriber to set aside the contract, to enjoin actions at law for calls, and to recover back payments made before discovery of the fraud.³ It is the customary, and,

R. 4 H. L. 64 (1869); aff'g L. R. 2 Eq. 264; *Etna Ins. Co. v. Shields*, Ir. R. 7 Eq. 264; *Bath's Case*, 8 Ch. Div. 334 (1878). See also *Fox's Case*, L. R. 5 Eq. 118 (1868). *Contra*, *Steel's Case*, 49 L. J. (Ch.) 176 (1879).

¹ Mere repudiation, not followed up by anything more, is insufficient. *Re Scottish Petroleum Co.*, L. R. 23 Ch. Div. 413 (1882), where the directors refused to allow the rescission. See also *Hare's Case*, L. R. 4 Ch. 503 (1869).

² "It is a good answer at common law to an action for calls, that the defendant was induced to become the holder of the shares by the fraud of the plaintiffs."

Bwlch-y-plwm Lead M. Co. v. Baynes, 36 L. J. (Ex.) 183 (1867); *Deposit Life A. Co. v. Ayscough*, 6 E. & B. 761 (1856); *Sandford v. Handy*, 23 Wend. 260 (1840).

³ But the injunction to restrain the action at law will not be granted if the subscriber delays until the case is about to be tried. *Thorpe v. Hughes*, 3 Myl. & Cr. 742. And where the stock has been fully paid, and no injury can come from the delay, equity will not sustain the subscriber's bill to compel repayment, but will send him to a court of law where a jury may pass upon the question of fraud. *Askew's Case*, L. R. 9 Ch. 664 (1874). Equity, however, unquestionably has concurred,

it seems, favorite remedy in England, and has been clearly upheld in this country.¹

§ 156. The complainant in a bill in equity to set aside a subscription obtained by fraud cannot sue in behalf of himself and others who may wish to come in. But several subscribers, defrauded in the same way, may join in the bill as co-complainants. The corporation is to be a defendant, and if merely a cancellation of the subscription and an injunction against suits at law are sought, the corporation, it seems, may be the sole defendant. A court of equity in these actions will give complete relief by decreeing that the directors guilty of the fraud shall refund to the subscriber payments made by him before discovering the fraud.³ This relief dispenses with an action at law for damages for deceit, and when sought for in the bill in equity, the guilty directors must be made parties. The bill is not multifarious by reason of its blending prayers for these various different kinds of relief.⁴

§ 157. *Remedy by an action at law for deceit.*—An action at law for damages for deceit lies at the instance of a subscriber for stock, fraudulently induced to subscribe, against the persons guilty of the fraud.⁵ The fraudulent representation, however, which must be proved to sustain this action, must be a more intentional fraud than the one which suffices to rescind the contract.

rent jurisdiction if it cares to exercise it. *Hill v. Lane*, L. R. 11 Eq. 215 (1870), criticising *Ogilvie v. Currie*, 37 L. J. 541 (1867). And will enjoin the collection of the subscription pending the suit. *Walsh v. Seager*, N. Y. Daily Reg., Sept. 3, 1886 (N. Y. Sup. Ct.). And the equitable action will not be enjoined merely because the corporation subsequently becomes insolvent, and a receiver is appointed. *Id.*, 1 N. Y. State Rep. 189 (June, 1886).

¹ *Waldo v. Chicago, St. P., &c., R. R. Co.*, 14 Wis. 575 (1861); *Henderson v. R. R. Co.*, 17 Tex. 560 (1856); *Rawlins v. Wickham*, 3 De G. & J. 304 (1858). And see the various English cases in this chapter.

² *Smith v. Reese River, &c., Co.*, L. R. 4 H. L. 64 (1869); *Hallows v. Fermie*, L. R. 3 Ch. App. 467 (1868). A transferee of the shares cannot bring the suit. The fraud is personal to the original subscriber. *Duranty's Case*, 26 Beav. 268 (1858).

³ *Vreeland v. N. J. Stone Co.*, 29 N. J. Eq. R. 188 (1878); *Reese River Silver Min. Co. v. Smith*, L. R. 4 H. L. 64 (1869).

⁴ Nor is it multifarious because it joins such a suit with one by the corporation to compel the directors to account to the corporation for the same fraud. *Ashmead v. Colby*, 26 Conn. 287 (1857).

⁵ *Clarke v. Dickson*, 6 C. B. (N. S.) 453 (1859); *Miller v. Barber*, 66 N. Y. 558 (1876); *Paddock v. Fletcher*, 42 Vt. 389 (1869). In England the liability of the directors herein is enforced generally in connection with a suit in equity, and as a part of the equitable decree. This is under a statute. *Western Bk. of Scotland v. Addie*, L. R. 1 Sc. App. Cas. 145. A false affirmation, made by the defendant with intent to defraud the plaintiff, whereby the plaintiff receives damage, is the ground of an action upon the case in the nature of deceit. In such an action it is not necessary that the defendant should be benefited by the deceit, or that he should collude with the person who is. 1 *Smith's Leading Cases* (8th Eng. ed.), 66-94, as applicable to misrepresentations inducing subscriptions.

The subscriber must prove that a material false misrepresentation was made by the defendant, that the defendant knew the representation to be false when he made it, that the plaintiff subscribed by reason, partially at least, of that representation, and that he was thereby injured.¹ The gist of the action is fraudulent intent.² It cannot be maintained against the corporation, because the corporation, though liable to refund fraudulently-acquired property, is not capable of a fraudulent intent.³

§ 158. The directors are not liable to an action for deceit by reason of the frauds of their agents,⁴ nor is an innocent director liable for the fraudulent representations of his co-directors, not even though the evidences of their fraud were entered on the corporate books, there being no ground for suspicion.⁵

A director cannot be held liable for false representations contained in the articles of association, which were made before he became a director.⁶ But a director who stands by and allows a co-director to make the false representations, is chargeable equally with the injury done thereby.⁷ The false representations supporting an action for deceit may have been by corporate reports or prospectuses, or by personal statements.

¹ *Ship v. Cresskill*, L. R. 10 Eq. Cas. 73 (1870). To sustain the action for deceit, the plaintiff must show "that the defendants intended that people should act on the statements, that the statements are untrue in fact, and that the defendants knew them to be untrue, or made them under such circumstances that the court must conclude that they were careless whether they were true or not;" also that the statements were relied upon, acted on, and damage sustained. *Edgington v. Fitzmaurice*, L. R. 29 Ch. D. 459 (1885).

² *Scienter* is fixed on the directors, making them liable in damages upon proof of incorrect representations, known to them to be incorrect, knowingly stated by them, and acted on by the plaintiff subscriber. *Henderson v. Lacon*, L. R. 5 Eq. Cas. 249 (1867); *Cargill v. Bower*, L. R. 10 Ch. D. 502 (1878). See also *Bale v. Cleland*, 4 F. & F. 117 (1864), and see p. 36, n. 3, *supra*. Must allege knowledge and intent to deceive on their part. "Falsely and fraudulently represented" does not properly plead the *scienter*. *Mahey v. Adams*, 3 Bosw. 346 (1858).

In case the representations are not fraudulent as against the corporation, they

are not sufficient to entitle the subscriber to recover from the directors. *Heymann v. European Central Ry. Co.*, L. R. 7 Eq. Cas. 154 (1868).

³ *Mixer's Case*, 4 De G. & J. 575; *Duranty's Case*, 26 Beav. 268 (1858); *Western Bk. of Scotland v. Addie*, L. R. 1 Sc. App. Cas. 145; *Abrath v. Northeastern Ry. Co.* 55 L. T. R. (N. S.) 63 (1886). *Contra*, *Peebles v. Patapsco Guano Co.*, 77 N. C. 233 (1877); *Barwick v. English Joint Stock Bk.*, L. R. 2 Ex. 259 (1867); *Mackay v. Com. Bk. of New Brunswick*, L. R. 3 P. C. 394, not stock cases, but distinctly holding that a corporation is liable to an action for damages for deceit.

⁴ *Weir v. Barnett*, 26 Week. Rep. 147 (1877); *Weir v. Bell*, L. R. 3 Ex. Div. 238 (1878); *Eaglesfield v. Marquis of Londonderry* (H. L.), 26 W. R. 540 (1878). See also *Cargill v. Bower*, L. R. 10 Ch. D. 502 (1878); *Watson v. Earl Charlemont*, 12 Q. B. 856 (1848); *Arthur v. Griswold*, 55 N. Y. 400 (1874).

⁵ *Re Denham & Co.*, L. R. 25 Ch. Div. 752 (1883).

⁶ *Mahey v. Adams*, 3 Bosw. 346 (1858).

⁷ *Vreeland v. N. J. Stone Co.*, 29 N. J. Eq. 188 (1878).

§ 159. *Remedy by action for money had and received.*—Where a subscriber pays his subscription in part or wholly, and afterwards discovers that the representations whereby he was induced to subscribe were fraudulent, he may bring an action at law for money had and received, and recover back from the corporation the money so received.¹ If the money has not yet passed into the hands of the corporation, he may recover it from the person who has it. If, however, he would be barred from suing in a court of equity by reason of his laches or corporate insolvency, he would fail, equally, in this remedy at law.

§ 160. *Ratification as a bar to the subscriber's remedies.*—A subscription contract obtained by fraudulent representations may cease to be voidable, and may become absolutely binding by acts of ratification. Any act of the subscriber, inconsistent with an intention to disaffirm the contract, will constitute a ratification of the subscription and a waiver of the right to avoid it by reason of fraud, provided the subscriber knew of the fraud at the time of such ratifying act. Thus, where the subscriber, after knowledge of the fraud, receives dividends,² sells part of the stock,³ instructs his broker to sell,⁴ participates in the meetings,⁵ pays calls,⁶ or, in general, accepts any corporate benefit or continues to act as a stockholder,⁷ he will be held to have waived all objections to the fraud, and to have ratified the subscription contract. But mere attendance at a stockholders' meeting,⁸ or demanding a dividend,⁹ or voting his shares by proxy,¹⁰ is insufficient.

¹ Grangers' Ins. Co. v. Turner, 61 Ga. 561 (1878); Hamilton v. Grangers' L. & H. Ins. Co., 67 Ga. 145 (1881). But the subscriber cannot retain the stock and also sue. Houldsworth v. City of Glasgow Bk., L. R. 5 App. Cas. 317 (1880). See Jarrett v. Kennedy, 6 C. B. 319 (1848). Assumpsit for money had and received brought against the directors to compel them to repay money paid on a subscription obtained by fraud, was sustained, without involving the question of a fraudulent intent.

² Scholey v. Central Ry. Co., L. R. 9 Eq. 266 n. (1870); Ayres' Case, 25 Beav. 513 (1858); Mixer's Case, 4 De G. & J. 575.

³ Ayres' Case, 25 Beav. 513 (1858).

⁴ *Ex parte* Briggs, L. R. 1 Eq. Cas. 483 (1866).

⁵ Harrison v. Heathorn, 6 Man. & G. 84 (1843); Chaffin v. Cummings, 37 Me. 76 (1853).

⁶ Scholey v. Central Ry. Co., L. R. 9 Eq. 266 n. (1870).

⁷ Ogilvie v. Knox Ins. Co., 22 Hun, 380; Chubb v. Upton, 95 U. S. 665 (1877); Litchfield Bk. v. Church, 29 Conn. 137 (1860); Kishacoquillas Centre Co. v. McCanahy, 16 S. & R. 140 (1827).

⁸ Stewart's Case, L. R. 1 Ch. App. 574 (1866); Wontner v. Shairp, 4 C. B. 404 (1847).

⁹ Phil. R. R. Co. v. Cowell, 28 Pa. St. 329 (1857).

¹⁰ McCully v. Pittsburgh, &c., R. R. Co., 32 Pa. St. 25 (1858); Greenville, &c., R. R. Co. v. Coleman, 5 Rich. L. 118 (1851).

§ 161. *Laches as a bar to the subscriber's remedies.*—Where a subscriber for stock, who was induced to subscribe by fraud, neglects for an unreasonable time after the discovery of the fraud to have his subscription cancelled, and, in the meantime, the interests of third persons became involved, and would be injured by the cancellation of such subscription, the subscriber's laches is a bar to relief, and a court of equity will refuse to set aside the subscription.¹ Equity does not allow the subscriber to say, "I will abide by the company, if successful, and I will leave the company, if it fails."² Immediately upon receiving information of the fraud, it is his duty to decide whether he will rescind the contract or waive the fraud.³ Nevertheless delay is not fatal, unless circumstances and third parties' rights have so changed or been acquired that the rescission would be inequitable. Consequently the decision of each case depends largely on the facts of the case. Thus it has been held that a delay of one,⁴ two,⁵ three,⁶ four,⁷ or six months,⁸ or of two⁹ or six¹⁰ years, was fatal under the circumstances of the case, while, under different facts, a delay of two months¹¹ and seven years¹² was held not to be a bar. In the remedies by actions at law, the Statute of Limitations governs, and, by analogy, courts of equity are inclined to follow the same period, unless there be an equitable reason to the contrary.

§ 162. The date from which laches begin to run is the time when the subscriber first is chargeable with notice that a fraud has been perpetrated upon him. Mere suspicions or random statements heard in public or in stockholders' meetings do not necessa-

¹ City Bk. of Macon v. Bartlett, 71 Ga. 797 (1888). As a bar in an action at law. Schwanck v. Morris, 7 Rob. (N. Y.), 658 (1868). But it is no bar that other subscribers may have been induced to subscribe by reason of this subscription. Western Bk. of Scotland v. Addie, L. R. 1 Scotch App. Cas. 145. Cf. Parbury's Case, 3 De G. & Sm. 43 (1849).

² Re London & Staffordshire Fire Ins. Co., L. R. 24 Ch. Div. 149 (1888); Ashley's Case, L. R. 9 Eq. Cas. 263 (1870).

³ Heymann v. European Central Ry. Co., L. R. 7 Eq. Cas. 154 (1868); Peek v. Gurney, L. R. 6 H. L. 377 (1873). The last case overrules Bagshaw v. Seymour, 18 C. B. 903 (1856), and Bedford v. Bagshaw, 4 H. & N. 538 (1859).

⁴ Taite's Case, L. R. 3 Eq. Cas. 795 (1867), the delay evidently being to see

which course would be most profitable. Peel's Case, L. R. 2 Ch. App. 674 (1867); Kincaid's Case, L. R. 2 Ch. 412 (1867).

⁵ Wilkinson's Case, L. R. 2 Ch. App. 536 (1867).

⁶ Heymann v. European Central Ry. Co., L. R. 7 Eq. Cas. 154 (1868).

⁷ Ex parte Lawrence, 36 L. J. (Ch.), 490 (1867).

⁸ Whitehouse's Case, L. R. 3 Eq. Cas. 790 (1867).

⁹ Farrar v. Walker, 3 Dill. 506 n.; Ashley's Case, L. R. 9 Eq. Cas. 263 (1870); three years, State v. Jefferson Turnpike Co., 3 Humph. (Tenn.), 305 (1842).

¹⁰ Denton v. Macneil, L. R. 2 Eq. 352 (1866).

¹¹ Directors, &c., of Central Ry. v. Kisch, L. R. 2 H. L. App. Cas. 99 (1870).

¹² McClellan v. Scott, 24 Wis. 81 (1869).

rily constitute notice.¹ But after a subscriber's suspicions are reasonably aroused, it is his duty to investigate at once.² The corporation has the burden of proof in asserting that the subscriber had notice and was guilty of laches.³

§ 163. *Corporate insolvency as a bar to the subscriber's remedies.*—In England the principle has become well established that after the statutory proceedings for winding up a corporation by reason of corporate insolvency have been commenced, a subscriber cannot rescind his subscription on account of fraud.⁴ He is too late. It matters not that he did not discover the fraud until after the winding up has commenced. The rights of corporate creditors prevail, then, over the equities of the subscriber.⁵ If, however, he commenced proceedings to rescind the contract before the winding up was commenced, he may be released, although the proceedings are not completed until after such winding up.⁶ So also where there are several similar cases, and by agreement between the corporate solicitors all the cases are to follow a test case, this agreement prevails, although a winding up is commenced before the test case was fully decided.⁷ The highest court in England in one case goes farther and intimates that corporate insolvency is a bar to rescission of a subscription for fraud, even though a winding up has not been commenced.⁸

§ 164. In this country the effect of corporate insolvency upon the right of a subscriber to rescind his contract for fraud has not

¹ *Directors, &c., of Central Ry. Co. v. Kisch*, L. R. 2 H. L. App. Cas. 99 (1870).

² *Ogilvie v. Currie*, 37 L. J. (Ch.) 541 (1867); *Ashley's Case*, L. R. 9 Eq. Cas. 263 (1870).

³ *Re London & S. F. Ins. Co.*, L. R. 24 Ch. Div. 149 (1883).

⁴ *Wright's Case*, L. R. 12 Eq. Cas. 331; *Kent v. Freehold, L. & B. M. Co.*, L. R. 3 Ch. App. 493 (1868); *Henderson v. Royal British Bk.*, 7 El. & Bl. 356 (1857); *Powis v. Harding*, 1 C. B. (N. S.) 533 (1857); *Daniell v. Off. Managers of Bk.*, 1 H. & N. 681 (1857); *Oakes v. Turquand*, L. R. 2 H. L. App. Cas. 325 (1867); *Mixer's Case*, 4 De G. & J. 575; *Clarke v. Dickson*, 27 L. J. (Q. B.) 223 (1858). So also where there is a voluntary winding up by reason of corporate insolvency. *Stone v. City & County Bk.*, L. R. 3 C. P. Div. 282 (1877); *Cullins v. Same, Id.* But not

if the proceedings for rescission were commenced in good faith and in ignorance of the winding up proceedings. *Hall v. Old. T. L. Min. Co.*, L. R. 3 Ch. D. 749 (1876).

⁵ *Turner v. Grangers, L. & H. Ins. Co.*, 65 Ga. 649 (1880).

⁶ *Reese River Co. v. Smith*, L. R. 4 H. L. 64 (1869); affirming s. c., L. R. 2 Ch. 604; L. R. 2 Eq. 264; reversing s. c., H. L. 36 L. J. (Ch.) 385.

⁷ *Pawle's Case*, L. R. 4 Ch. 497; *McMill's Case*, L. R. 10 Eq. 503 (1870). But mere attendance at the meeting where such stipulation is made is insufficient. The subscriber must plainly indicate an intention to abide by the test case. *Ashley's Case*, L. R. 9 Eq. Cas. 263 (1870).

⁸ *Tennent v. City of Glasgow Bk.*, L. R. 4 App. Cas. 615. See also *Burgess' Case*, L. R. 15 Ch. D. 507.

been so clearly determined. The decided tendency of the decisions, however, is that corporate insolvency is a bar to such rescission.¹ In the bankruptcy courts, under the late bankruptcy law, such a rule was upheld.²

§ 165. *Essential allegations in legal proceedings to remedy a fraud inducing subscription.*—The essential allegations, especially in a suit in equity, necessarily vary according to the peculiar facts of each case. Yet there are certain elements common to all the cases. It is necessary to allege that a material misrepresentation of a question of fact was made, setting out fully the fact misrepresented; that the person making the misrepresentation thereby bound the corporation; that the subscriber was thereby induced to make the subscription; and that upon discovery of the fraud, he immediately disaffirmed the contract.³ That the representation was false cannot be proved by statements made by the directors in stockholders' meetings.⁴ The burden of proving that the representation was false, and that the subscriber relied thereon, is upon the subscriber.⁵

¹ *Ruggles v. Brock*, 6 Hun, 164 (1875); *Saffold v. Barnes*, 39 Miss. 399 (1860). In *Chubb v. Upton*, 95 U. S. 665, 667 (1877), the court says it has often been held that the defense of false and fraudulent representations will not prevail against a receiver, especially where there has not been a prompt discovery of the fraud, followed by a repudiation, citing *Upton v. Tribilcock*, 91 U. S. 45 (1875); *Webster v. Upton*, Id. 65 (1875); *Sanger v. Upton*, Id. 56 (1875); *Ogilvie v. Knox Ins. Co.*, 22 Hun, 380. Cf. *Litchfield Bk. v. Peck*, 29 Conn. 384 (1860).

² *Farrar v. Walker*, 13 Natl. Bankr. Reg. 82 (1876); *Michener v. Payson*, Id. 49 (1876).

³ *Bwlch-y-plwm L. M. Co. v. Baynes*, 36 L. J. (Ex.) 183; *Deposit Life A. Co. v. Ayscough*, 6 E. & B. 761 (1856); *Upton v. Englehart*, 3 Dill. 496 (1874); *Hallows v. Fermie*, L. R. 3 Ch. App. 467 (1868);

Selma, M. & M. R. R. Co. v. Anderson, 51 Miss. 829 (1876). The last case holding it necessary to allege also that the fact misrepresented was not a charter matter. *Carey v. Cin. & Chicago R. R. Co.*, 5 Iowa, 357 (1857), indicates that an allegation that the certificates are brought into court for disposal is proper. See also *Oregon Central R. R. Co. v. Scoggin*, 3 Oreg. 161 (1869).

⁴ *In re Devala Prov. G. M. Co.*, L. R. 22 Ch. Div. 593 (1883). Cf. *Phil. W. & B. R. R. Co. v. Quigley*, 21 How. 202 (1858). *Contra*, *Jarrett v. Kennedy*, 6 C. B. 319 (1848).

⁵ *Jennings v. Broughton*, 22 L. J. (Ch.) 585 (1853). In New York, proof of other similar contemporaneous frauds is admissible. *Miller v. Barber*, 66 N. Y. 558 (1876). In Alabama it is not admissible. *Montgomery S. Ry. Co. v. Matthews*, 77 Ala. 357 (1884).

CHAPTER X.

MISCELLANEOUS DEFENSES TO SUBSCRIPTIONS FOR CAPITAL STOCK.

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| § 166. Defenses to subscriptions not favored by the courts. | § 188. Fraud and mismanagement of directors. |
| 167-70. Release, withdrawal, cancellation, or rescission. | 189. Delay and abandonment of enterprise. |
| 171. Compromise. | 190. Failure of corporate enterprise. |
| 172-75. Non-payment of percentage required by statute. | 191. Other subscribers released. |
| 176-81. Full capital stock not subscribed. | 192. No certificates of stock issued. |
| 182. Capital stock not definitely resolved upon. | 193-94. Set-off and counterclaim. |
| 183-86. Irregular incorporation. | 195. Statute of limitations. |
| 187. <i>Ultra vires</i> acts. | 196. Ignorance or mistake. |
| | 197. Miscellaneous defenses. |
| | 198. Waiver of defenses. |

§ 166. *Defenses to subscriptions not favored by the courts.*—

It is a common saying and well recognized fact that the subscribers to certain corporate enterprises, especially railroads, rarely realize a profit from their investment, but, on the contrary, lose the whole amount of the subscription which they have made. These subscriptions are generally not called in until after corporate insolvency has occurred. Then the reluctance of the subscriber to pay a subscription from which there is no hope of a return, leads him to seek out and build up all possible defenses to defeat any action for the collection of the amount due from him. Some of these defenses are just, and have been sustained. But most of them have not been allowed. On the theory that having taken the chances of large gains, the subscriber takes also the risk of total loss, and that the hardship of the subscriber is not equal to the superior equities and rights of corporate creditors, the courts have uniformly discountenanced such defenses, and have rigidly enforced the subscriber's liability.

§ 167. *Release, withdrawal, surrender, cancellation, rescission.*—These terms are frequently used as synonymous, although technically they have different meanings. The term release especially has led to considerable confusion. It has been applied to cases where the subscriber withdraws his offer to subscribe,

the contract not yet having been closed;¹ second, to cases where the subscriber retains his stock, but is not required to pay the full par value thereof;² third, to cases where the subscription contract is dissolved by mutual agreement, the subject of this section. The term rescission is more properly applied to the defense of fraudulent representations.³ Probably the term cancellation describes more accurately the dissolution of a subscription contract by the mutual consent of all parties concerned.⁴

§ 168. A subscription contract, like any other contract, may be waived, cancelled, or dissolved by the mutual consent of all the parties interested. The interested parties are the subscriber himself, the other stockholders and corporate creditors existing at the time of the cancellation. Frequently the directors of the corporation attempt to usurp this right and power of the general stockholders. The well established rule, however, is that corporate directors have no power to agree with a subscriber that his subscription shall be cancelled, unless such power is given to them by charter or statute, or the by-laws of the corporation.⁵

¹ For this class of cases see Ch. IV.

² For this class of cases see Ch. III.

³ See Ch. IX.

⁴ In Green's Brice's *Ultra Vires* (2d ed.), 181, a surrender is defined to be "the transfer by a member of his interest, whole or partial, in a company, to the company or to trustees for or nominees of it." See also *Re Dronfield Silkstone Coal Co.*, L. R., 17 Ch. D. 76 (1880); *Colville's Case*, 48 L. J. (Ch.) 633 (1879). A cancellation is defined, p. 189, to be "the capacity, after shares are allotted and accepted, when no dispute exists as to the liability of the shareholder to cancel such shares and determine the liability thereon. This must not be confused with the closely allied proceedings, (1) compromise of disputes, and (2) rescission of what has been wrongly done by inadvertence." As a matter of fact this dissolution of the subscription contract differs very little from an ordinary transfer of the shares to the corporation itself, except in the fact that by the former process all liabilities of the subscriber is ended absolutely. Cancellation cannot be objected to on the ground that it reduces the capital stock. It no more reduces the capital stock than a forfeiture does. *Re Dronfield Silkstone Coal Co.*, *supra*.

⁵ In the case of *Bedford R. R. Co. v. Bowser*, 48 Pa. St. 29, where just before the expiration of their office, the directors fraudulently released part of the subscribers, the court said: "It is an abuse of their trust wholly unauthorized, and at war with the design of the charter to single out some of the stock subscribers and release them from their liability. No such authority in them has ever been recognized." To the same effect, *Rider v. Morrison*, 54 Md. 429 (1880); *Hughes v. Antietam Mfg. Co.*, 34 Md. 316 (1870); *Ryder v. Alton, &c.*, R. R. Co., 13 Ill. 516 (1851); *Esparto Trading Co.*, L. R., 12 Ch. D. 191 (1879); *Hall's Case*, L. R., 5 Ch. 707; *Re London & Prov. Consol. Coal Co.*, L. R., 5 Ch. D. 525 (1877); *Re Argyle C. & C. Co.*, *Ex parte* Watson, Law Times, April 17, (1886); *Ex parte Fletcher*, 37 L. J. (Ch.) 49 (1867); *Addison's Case*, L. R., 5 Ch. 294; *Spackman v. Evans*, L. R., 3 H. L. 171 (1868); *Thomas's Case*, L. R., 13 Eq. 437 (1872), where the directors had power to "enter into, alter, rescind, or abandon contracts." *Richmond's Case*, 4 K. & J. 305 (1858), holding that power to forfeit does not give power to cancel. *Adam's Case*, L. R., 13 Eq. 474 (1872), holding that power to compromise gives no power to cancel. "It would be putting into the

§ 169. A subscriber for stock in a corporation cannot obtain a cancellation of his subscription except by the unanimous consent of the other subscribers.¹ Even a majority of the stockholders cannot withdraw and refuse to proceed.² The consent of all the other stockholders, however, need not be express.

If the means of notice are sufficient, so as to raise a clear presumption of knowledge and acquiescence, and the arrangement is left unimpeached by any one for many years, no objection can be made. The stockholders are bound by the cancellation.³ Where a subscription has been cancelled and calls already paid

hands of directors an almost unlimited power. . . . It might happen in cases where it would be impossible to fix fraud on them." Cf. *Plate Glass Ins. Co. v. Sunley*, 8 El. & Bl. 47 (1857); *Kollman's Carriage Co. v. Beresford*, 2 M. & G. 197; *Lord Belhaven's Case*, 34 L. J. (Ch.) 503; *Ex parte Blake*, 32 L. J. (Ch.) 278; *Dixon's Case*, 17 W. R. 1036; *Burt v. Farrar*, 24 Barb. 518 (1857); *Gregory v. Lamb*, 16 Neb. 205 (1884); *Erskine v. Peck*, 83 Mo. 465 (1884). See also § 153. The express power of the directors to do all things "conducive to the attainment of the objects for which it was established," does not enable them to agree to a cancellation. *Re Dronfield Silkstone Coal Co.*, L. R., 17 Ch. D. 76 (1880). Cannot be cancelled by a corporate solicitor, although the work, in which the subscription is due can no longer be done. *Wheatcroft's Case*, 29 L. T. 324 (1873). Sometimes the directors agree in advance to release or cancel a part or all of the subscriber's contract. Such agreements are void, not only as *ultra vires*, but as frauds on other subscribers. *Melvin v. Lamar Ins. Co.*, 80 Ill. 446 (1875); *Robinson v. Pittsburgh & Connellsville R. R. Co.*, 32 Pa. St. 334; *Minor v. Bk. of Alexandria*, 1 Pet. 65; *Jewett v. Valley Ry. Co.*, 34 O. St., 601 (1878); *White Mts. R. R. Co. v. Eastman*, 34 N. H. 124. See also *Pickering v. Templeton*, 2 Mo. App. 425; *Downie v. White*, 12 Wis. 176; *Blodgett v. Morrill*, 20 Vt. 509; *Davidson's Case*, 3 De G. & S. 21; *Bridger's Case*, L. R., 9 Eq. 74; *Litchfield Bank v. Church*, 29 Conn. 137. Where, however, the issue itself is *ultra vires*, being fictitious paid up stock, the directors may agree to a cancellation. *Barnett's Case*, L. R., 18 Eq. 507 (1874). Or an *ultra vires* stock dividend, *Hollingshead v. Woodward*,

35 Hun, 410 (1885). They may cancel it for mistake in registering the wrong man. *Ex parte Knightley*, W. M. (1874) 18 & 47. See also *Hartley's Case*, L. R., 10 Ch. 157. In England, an express power given by the articles of associations of the corporation may authorize cancellation by the directors. *Colville's Case*, 48 L. J. (Ch.) 633; *Snell's Case*; *Wright's Case*, L. R., 12 Eq. 334; *Teasdale's Case*, L. R., 9 Ch. 54.

¹ *Kidwelly Canal Co. v. Raby*, 2 Price, 93 (1816); *Lake Ontario, &c., R. R. Co. v. Mason*, 16 N. Y. 451, 463 (1857); *Hughes v. Antietam Mfg. Co.*, 34 Md. 316 (1870); *Johnson v. Wabash & Mt. Vernon P. R. Co.*, 16 Ind. 389 (1861); *United Soc. v. Eagle Bk.*, 7 Conn. 457 (1829); *Bishop's Fund v. Eagle Bk.*, Id. 476; *Selma & Tenn. R. R. Co. v. Tipton*, 5 Ala. (N. S.) 787. See also *Cook v. Chittenden*, 25 Fed. Rep. 544, upholding a withdrawal. The plea in defense need not allege that the other stockholders assented to the cancellation. *Gelpcke v. Blake*, 19 Iowa, 263. Where, however, by the articles of association, acts of the directors ratified at stockholders' meetings were to be valid, a cancellation so ratified is legal and the unanimous consent is not necessary. *Marshall v. Glamorgan Iron & Coal Co.*, L. R., 7 Eq. 129 (1868).

² *Busey v. Hooper*, 35 Md. 15.

³ *Evans v. Smallcombe*, L. R., 3 H. L. 249. So also where the corporation retains the benefits of a cancellation, no objection can be made. *Miller v. Second J. B. Assn.* 50 Pa. St. 32. Proof of cancellation need not necessarily be by the corporate records. May be proved by evidence that the subscriber was not regarded "by himself or by the company, as a stockholder." *Stuart v. Valley R. Co.*, 32 Gratt. 146.

are refunded without the consent of the other stockholders, any stockholder may, by a bill in equity, have the money refunded to the corporation, and the subscriber made liable upon his cancelled subscription.¹ Moreover, the directors are personally liable to the corporation for loss occasioned by their improper cancellation of subscriptions.² When, however, a subscriber fails to pay his subscription or exercise his rights, it has been held that the corporation may treat his subscription as abandoned, and allow others to fill it.³

§ 170. A cancellation of a subscription, to the detriment of corporate creditors, may be impeached by the latter and set aside.⁴ Especially is this the rule, when the cancellation is made after the corporation has become insolvent.⁵ In the United States courts it is established that the governing officers of a corporation cannot, by agreement or other transaction with the stockholder, release the latter from his obligation to pay, to the prejudice of its creditors, except by fair and honest dealing, and for a valuable consideration.⁶

§ 171. *Compromise*.—A compromise differs from a cancellation, in that the subscriber pays to the corporation a part of the subscription price, in order to be released from the balance. The stock is delivered back to the corporation. The corporate authorities, generally the directors, have power to compromise any corporate debt, and if, in the collection of subscriptions, there is reasonable doubt as to the liability of the subscriber,⁷ or

¹ *Melvin v. Lamar Ins. Co.*, 80 Ill. 446.

² *Hodgkinson v. Natl. Co.*, 26 Beav. 473; *Bk. of St. Mary's v. St. John*, 25 Ala. 566.

³ *Perkins v. Union B. H. & E. M. Co.*, 12 Allen, 273. Cancellation may be by the subscription of another person for the subscriber at the latter's request. This occurs where regular transfer is not yet possible. The signature of the first subscriber must be erased, and that of his substitute inserted. Otherwise the substitution fails. *Ryder v. Alton & S. R. R. Co.*, 13 Ill. 516, and see § 75.

⁴ One who is a corporate creditor before the cancellation is made may object to it, *Vick v. LaRochelle*, 57 Miss. 602. But not if the debt was incurred after the cancellation. *Johnson v. Sullivan*, 15 Mo. App. 55; *Erskine v. Peck*, 18 Mo.

App. 280. The plea in defense, it has been held, need not allege that there were no corporate creditors at the time of the cancellation. *Gelpcke v. Blake*, 19 Iowa, 263. In England a different rule prevails. "If the company could not question it, neither can a creditor, for he can obtain nothing but what the company can get from the shareholders." *Re Dronfield Silkstone Coal Co.*, L. R. 17 Ch. D. 76 (1880).

⁵ *Chouteau Ins. Co. v. Floyd*, 74 Mo. 286; *Gill v. Balis*, 72 Mo. 424, holding also that it is immaterial that enough subscriptions remain to pay the corporate debts.

⁶ *Burke v. Smith*, 16 Wall. 390 (1872); *New Albany v. Burke*, 11 Wall. 96 (1870). So also in Illinois. See *Zirkel v. Joliet Opera House Co.*, 79 Ill. 334 (1875).

⁷ *Bath's Case*, L. R., 8 Ch. D. 334

if the subscriber is insolvent, the corporation may compromise the liability, and release a part for the purpose of securing the residue. All that is required is good faith.¹ A receiver, however, cannot compromise a subscription, nor can a court of equity give him power so to do, at least, it cannot, unless all the stockholders are parties to the equitable suit in connection with which the receiver is appointed.²

§ 172. *Non-payment of a percentage required by statute.*—

The charter or statute governing a corporation often prescribes, that each subscriber to the capital stock shall, at the time of subscribing, pay to the corporation a fixed sum or a specified proportion of the subscription. These statutes vary somewhat in their provisions, some declaring the subscription to be void unless the percentage is paid, others merely prescribing that it shall be paid.

In the actual taking of the subscriptions, it frequently happens that the subscriber has not the ready money requisite, and is allowed to subscribe without paying the same. When an attempt is made to collect such a subscription, the subscriber, if the enterprise has resulted disastrously, sets up the defense that he did not pay the statutory percentage, and that the subscription is void and not enforceable. A long list of cases, dating from the early litigation over railroads, have turned upon this defense. In some of the States the defense has been held insufficient, in others a contrary rule prevails, and in still others, first one rule and then the other has been adopted.

§ 173. The decided weight of authority and the most carefully considered cases hold that a subscriber for stock cannot escape the responsibilities of a stockholder by showing that he never paid the percentage or fixed amount required by charter or statute to be paid at the time of subscribing.³ He will not thus be

(1878); Lord Belhaven's Case, 3 De G., J. & S. 41 (1865).

¹ Phil. & W. C. R. R. Co. v. Hickman, 28 Pa. St. 318 (1857). Power may be given by statute. Pearson's Case, L. R., 7 Ch. 309, holding that under the English statute, the court may allow, but cannot compel, a receiver to compromise.

² Chandler v. Brown, 77 Ill. 333 (1875).

³ Illinois River R. R. Co. v. Zimmer, 20 Ill. 654 (1858), holding that the commissioners may waive payment. The

court says: "This indulgence is a most ungracious defense, which should not be allowed unless it is strictly required by some inflexible rule of law." Haywood & P. P. R. Co. v. Bryan, 6 Jones' L. (N. C.) 82 (1858), the court saying: "It would be a strange rule which would allow him to take advantage of the other stockholders' forbearance and his own neglect." Pittsburgh, W. & K. R. R. Co. v. Applegate, 21 W. Va. 172 (1882). On the theory that the statute is "to insure good

permitted to take advantage of his own wrong and default to the prejudice of others. In some instances the percentage was paid in notes¹ or checks,² instead of cash; in others, payment in cash was made at some period subsequent to the act of subscribing³; in still others, no payment at all was made on the subscription, and suit was brought for the whole amount.⁴ In England, a

faith, and to avoid shams in enterprises that so vitally affect the public," but not to change the liability of stockholders to corporations. *Minnesota & St. L. Ry. Co. v. Bassett*, 20 Minn. 535 (1874), where the court said of the statute: "While it confers upon plaintiff the right to insist upon the payment, it does not make the successful exercise of this right indispensable to the validity of the subscription." *Water Valley Mfg. Co. v. Seaman*, 53 Miss. 655 (1876), where the requirement was provided for in the subscription itself. *Barrington v. Miss. C. R. R. Co.*, 32 Miss. 370 (1856), where payment was made before the subscription. See also *Vicksburg S. & T. R. R. Co. v. McKean*, 12 La. Ann. 638 (1857); *Wight v. Shelby R. R. Co.*, 16 B. Monr. (Ky.) 4 (1855); *Smith v. Plankroad Co.*, 30 Ala. 650 (1857); *Mitchell v. Rome R. R. Co.*, 17 Ga. 574 (1855); *Henry v. Vermillion & A. R. R. Co.*, 17 O. 191 (1848); *Chamberlain v. Painesville & H. R. R. Co.*, 15 O. St. 225 (1864); *Napier v. Poe*, 12 Ga. 170 (1852); *Fiser v. Miss. & Tenn. R. R. Co.*, 32 Miss. 359; *Ryder v. Alton & S. R. R. Co.*, 13 Ill. 516, where the subscriber was one of the commissioners. *Klein v. Alton & S. R. R. Co.*, 13 Ill. 514, where payment was made before the subscription books were closed. *Stuart v. Valley R. R. Co.*, 32 Gratt. (Va.) 146; *Southern L. Ins. Co. v. Lanier*, 5 Fla. 110 (1853); *Selma & Tenn. R. R. Co. v. Roundtree*, 7 Ala. (N. S.) 670 (1845); *Spartanburg & A. R. R. Co. v. Ezell*, 14 S. C. 281 (1880), where a few subscribers paid in more than their percentage, and enough to make up for those not paying. *Oler v. Baltimore R. R. R. Co.*, 41 Md. 583 (1874), where the percentage was "payable," the court saying that this merely made it "due and collectible," like a call. To same effect, *Ashtabula & N. L. R. R. Co. v. Smith*, 15 O. St. 328 (1864). Payment by the subscriber's agent is sufficient. *Litchfield Bk. v. Church*, 29 Conn. 137 (1860). The following cases hold that non-payment of the required percentage is a good defense. *Charlotte & S. C. R. R. Co. v. Blakely*, 3

Strobb. Eq. (S. C.) 245 (1848); *State Ins. Co. v. Redmond*, 1 McCrary, 308 (1880). The requirement herein was by by-law. *People v. Chambers*, 42 Cal. 201 (1871), holding a check to be insufficient. *Farmers' & M. Bk. v. Nelson*, 12 Md. 35 (1857); *Taggart v. Western Md. R. R. Co.*, 24 Md. 588 (1866); *Wood v. Coosa & C. R. R. Co.*, 32 Ga. 273 (1861). The statute prescribing that the subscription shall be "void."

¹ *Vt. Central R. R. Co. v. Claves*, 21 Vt. 30 (1848). A bond so given is collectible, as it would be if given to carry out a parol contract for the sale of land void by Statute of Frauds. *McRea v. Russell*, 12 Ired. (N. C.) 224 (1851), the court saying that the statute "was meant to protect stockholders from men of straw. It was, moreover, meant to protect men from the consequences of making such subscriptions under the influence of momentary excitement, which they could not fulfil." The statute said the subscription should be void. In the case, *Home Stock Ins. Co. v. Sherwood*, 72 Mo. 461 (1880), payment by note and mortgage was sustained. *Hayne v. Beauchamp*, 13 Miss. 515 (1846), holding that the payment by note amounted to an informal subscription, the statutory subscription being void. *Pine River Bk. v. Hadsdon*, 46 N. H. 114 (1865).

² *People v. Stockton & V. R. R. Co.*, 45 Cal. 306 (1873), there being funds in the bank to meet it.

³ Payment of a judgment on an action for one call estops the subscriber from setting up this defense. *Hall v. Selma & Tenn. R. R. Co.*, 6 Ala. (N. S.) 741 (1844).

⁴ In the case *Piscataqua Ferry Co. v. Jones*, 39 N. H. 491 (1859), the requirement was by by-law, not by charter. The subscription was to be void for non-payment. The court thought otherwise. The effect of non-payment is that "it is due and liable to be called for at any time—payable on demand, whenever needed by the corporation." *Greenville & C. R. R. Co. v. Woodsides*, 5 Rich. L. (S. C.) 145 (1851), where the subscriber also voted the stock.

failure to pay such a percentage is held not to affect the liability of the subscriber, but to restrict his right of transferring his stock.¹

§ 174. In New York there has been doubt and a strong tendency to change the rule laid down at an early day by the court. The case of *Jenkins v. The Union Turnpike Company*, in 1804,² decided that a failure by the subscriber to pay a required percentage at the time of subscribing was a good defense to an action on the subscription. This decision has been distinguished, questioned, and doubted by the courts.³ The latest authority, however, in New York, undoubtedly holds that if the subscriber merely signs the subscription contract, and does not pay the per-

¹ *East Gloucestershire Ry. Co. v. Bartholomew*, L. R. 3 Ex. 15 (1867); *Purdy's Case*, 16 W. R. 660 (1868); *McEwen v. West. L. W. & W. Co.*, L. R. 6 Ch. 655 (1871). The statute stating that the stock should not "issue" or "vest" until one fifth should be paid. See also *Morton's Case*, L. R. 16 Eq. 104 (1873).

² 1 *Caine's Cases in Error*, 86, reversing *Union Turnpike Co. v. Jenkins*, 1 *Caine's Rep.* 381.

³ *Highland Turnpike Co. v. McKean*, 11 Johns. 98 (1814), the court saying: "It is a little difficult to ascertain the point upon which the Court of Errors grounded their decision." A subscriber, who is also the commissioner, need not pay the required percentage to himself. In *Crocker v. Crane*, 21 Wend. 211 (1839), payment in checks was held not to be good, they evidently not having been given in good faith. The court says: "Receiving an occasional check might have been a fair substitute." *Thorp v. Woodhull*, 1 Sandf. Ch. 411 (1844), sustains the validity of a bond and mortgage in payment of a subscription in which the percentage had been paid by a worthless check. *Eastern Plank Road Co. v. Vaughan*, 14 N. Y. 546 (1856), holds it not to be necessary "that each subscriber should pay five per cent. upon his subscription, but only that five per cent. on the amount of the stock subscribed should be actually paid [by any one]. The object of this provision plainly was to prevent the formation of corporations and cumbering the records of the State, without some evidence that the contemplated enterprise is to be really prosecuted." To the same effect, *Lake Ontario A. & N. Y. R. R. Co. v. Mason*, 16 N. Y. 451

(1857), the court saying that the object was "to insure the organization of real substantial companies in good faith, animated by an honest purpose, and having some degree of ability at least to undertake the proposed improvement." In the case *Rensselaer & W. P. R. Co. v. Barton*, 16 N. Y. 457 (n.), the court, in speaking of the decision in *Jenkins v. Union T. Co.*, says: "It may well be doubted whether the reasoning upon which it was based is sound, and whether, were the question to be again directly presented, this court would feel bound to follow it." *Black River & Union R. R. Co. v. Clarke*, 25 N. Y. 208 (1862), holds that "the subscription one day, with payment the next, would satisfy the statute, and so would actual payment at any period after subscription with intent to effectuate and complete the subscription." See also *Beach v. Hazard*, as stated in 30 N. Y. 118; *Ogdensburgh, C. & R. R. Co. v. Wooley*, 3 Abb. Ct. of App. 398 (1864), holds that the requisite percentage for all may be paid by a few subscribers, and that a promissory note is good payment. *Beach v. Smith*, 30 N. Y. 116 (1864), affirming s. c. 28 Barb. 254, holds that payment in services performed under a contract with the company suffices. *Excelsior G. B. Co. v. Stayner*, 25 Hun, 91 (1881), holds that payment by check, on which payment is stopped, is insufficient. *Syracuse, P. & O. R. R. Co. v. Gere*, 4 Hun, 392 (1875), sustains a suit by the corporation to collect such a check. See also *Ogdensburgh R. & C. R. R. Co. v. Frost*, 21 Barb. 541 (1856). Certified check is good payment. *Re Staten I. R. T. R. R. Co.*, 37 Hun, 422 (1885); 38 Hun, 381.

centage, he may thereby defeat his liability on such subscription.¹

§ 175. In Pennsylvania a similar state of doubt has existed. The case of *Hibernia Turnpike Co. v. Henderson*,² in 1822, decided that a failure by the commissioners taking subscriptions to stock to require payment of the statutory percentage made the subscription void and not enforceable. Later decisions do not overthrow the rigid rule, but distinguish and practically destroy it by holding that this defense is barred by a subsequent statute curing the defect;³ or by a waiver in attending corporate meetings and voting;⁴ or by transferring the shares;⁵ or that the provision applies only to subscriptions taken by the commissioners;⁶ or under the act of 1868, that the percentage must be paid on subscriptions after, but not to those before incorporation;⁷ or that the requirements does not apply to a conditional subscription;⁸ or any acts indicating an intent to be bound as a stockholder.⁹

§ 176. *Failure of the corporation to obtain subscriptions to the extent of the full capital stock.*—It is an implied part of a contract of subscriptions that the contract is to be binding and enforceable against the subscriber only after the full capital stock of the corporation has been subscribed. This condition precedent to the liability of the subscriber need not be expressed in the corporate charter nor the subscription itself. It arises by implication from the just and reasonable understanding of a sub-

¹ *New York & O. M. R. R. Co. v. Van Horn*, 57 N. Y. 473 (1874), holding also that a subsequent statute cannot cure such omission to pay, and thereby render the subscriber liable.

² 8 S. & R. 219. See also *Leighty v. Pres. of S. & W. T. Co.*, 14 S. & R. 434.

³ *Clark v. Monongahela Nav. Co.*, 10 Watts, 364 (1840).

⁴ *Erie & W. P. R. Co. v. Brown*, 25 Pa. St. 156 (1855). The court saying: "There is no merit in such a defense. . . . The subscriber himself is under the highest moral obligations faithfully to perform the promise he has distinctly made." In the case of *Cam v. Westchester R. R. Co.*, 3 Grant's Cas. 200 (1855), the court held that failure to pay the percentage did not render the charter forfeitable.

⁵ *Everhart v. Westchester & Phil. R. R. Co.*, 28 Pa. St. 339 (1857).

⁶ *Phil. & W. C. R. R. Co. v. Hickman*, 28 Pa. St. 318 (1857). *Contra*, under the act of 1868. See *Butcher v. Dillsburg & M. R. R. Co.*, 76 Pa. St. 306 (1874).

⁷ *Garrett v. Dillsburg & M. R. R. Co.*, 78 Pa. St. 465 (1875).

⁸ *Hanover J. & S. R. R. Co. v. Halde- man*, 82 Pa. St. 36 (1876).

⁹ *Boyd v. Peach. B. Ry. Co.*, 90 Pa. St. 169 (1879). Holding, however, that payment cannot be by promissory note, although a demand note. The court said: "The manifest object of the requirement was to protect the public against fictitious corporations, with capital stock subscribed perhaps by irresponsible persons, and not a dollar thereof paid or intended to be paid in."

scriber that he is to be aided by other subscriptions. This rule is supported also by public policy, in that corporate creditors have a right to rely upon a belief that the full capital stock of the corporation has been subscribed.¹ The subscriber, however, is liable for his proportion of the necessary expenses, preliminary to the incorporation and organization of the company.²

§ 177. The act of incorporation may, of course, vary this rule. Thus, it is well established, that where the charter authorizes the organization of the company, and the commencement of

¹ The leading case on this defense is *Salem Mill Dam Corporation v. Ropes*, 23 Mass. 23 (1827), and 26 Mass. 187 (1829); *Livesey v. Omaha Hotel*, 5 Neb. 50 (1876), where Judge Redfield in the brief says: "This rule has been held inflexible in all cases both for the security of the public and also of the subscribers." *Shurtz v. Schoolcraft & T. R. R. Co.*, 9 Mich. 269 (1861); *New York, H. & N. R. R. Co. v. Hunt*, 39 Conn. 75 (1872); *Hale v. Sanborn*, 16 Neb. 1 (1884); *Peoria & R. I. R. R. Co. v. Preston*, 35 Iowa, 118 (1872), the court saying that this rule, "unless a contrary intention appears, expressly or by implication, either in the charter or the contract of subscriptions." *Stoneham Branch R. R. Co. v. Gould*, 68 Mass. 277 (1854), the court saying: "This is no arbitrary rule, it is founded on a plain dictate of justice, and the strict principles regulating the obligation of contracts." *Bray v. Farwell*, 81 N. Y. 600, 608 (1880), where the court says, the directors "had no authority to go on with insufficient means and thus wreck the company." *Selma, M. & M. R. R. Co. v. Anderson*, 51 Miss. 829 (1876); *Hughes v. Antietam Mfg. Co.*, 34 Md. 318, 332 (1870); *Topeka Bridge Co. v. Cummings*, 3 Kan. 55 (1864); *Allman v. Havana R. & E. R. R. Co.*, 88 Ill. 521 (1878); *Temple v. Lemon*, 112 Ill. 51 (1884); *Littleton Mfg. Co. v. Parker*, 14 N. H. 543 (1844); *Hendrix v. Academy of Music*, 73 Ga. 437 (1884); *Contoocook Valley R. R. Co. v. Barker*, 32 N. H. 363 (1854); *Prop. of N. Bridge v. Story*, 6 Pick. 45 (1827); *Belfast & M. L. R. R. Co. v. Cottrell*, 66 Me. 185 (1875); *Memphis Branch R. R. Co. v. Sullivan*, 57 Ga. 240; *Fox v. Allensville C. S. & V. T. Co.*, 46 Ind. 31 (1874); *Hain v. North W. G. R. Co.*, 41 Ind. 196 (1872), holding also that the corpora-

tion in suing must aver that the full capital stock has been subscribed. *Central Turnpike Co. v. Valentine*, 10 Pick. 142 (1830), holding also that the corporation has the burden of proving subscriptions for the full capital stock. *Warwick R. R. Co. v. Cady*, 11 R. I. 131 (1877), where the charter said that the capital stock should not exceed a specified sum. *Fry's Exrs. v. Lexington & B. S. R. R. Co.*, 2 Met. (Ky.) 314 (1859). Holding also that the corporation must aver full subscription. *Lewey's Island R. R. Co. v. Bolton*, 48 Me. 451 (1860); *Lail v. Mt. Sterling C. R. Co.*, 13 Bush (Ky.), 34 (1877), holding that the corporation need not aver full subscriptions. *Cf. Monroe v. Fort W. J. & S. R. R. Co.*, 28 Mich. 272 (1873). Where also the corporation is incorporated with a less capital stock than was proposed when the defendant subscribed, he is not bound by the subscription. *Santa Cruz R. R. Co. v. Schurtz*, 53 Cal. 106 (1878). A few cases seem to hold a contrary doctrine. *New Castle & A. T. Co. v. Bell*, 8 Blackf. (Ind.) 584 (1847); *Oregon Central R. R. Co. v. Scoggin*, 3 Oreg. 161 (1869); *York & C. R. R. Co. v. Pratt*, 40 Me. 447 (1855); *Cheraw & C. R. R. Co. v. White*, 10 S. C. 155 (1878). See also *Chubb v. Upton*, 95 U. S. 665, 668 (1877), probably a dictum. In the late case of *Skowhegan & A. R. R. Co. v. Kinsman*, 77 Me. 370 (1885), the court seems to hold that where there is in the subscription an express promise to pay, it is enforceable, even though the whole capital stock is not subscribed. If such a condition is expected the court says it must be inserted in the subscription. But see *Rockland, &c., B. Co. v. Sewall*, 12 Am. & Eng. Corp. Cas. 85 (Me. 1886).

² *Salem Mill Dam Corp. v. Ropes*, 23 Mass. 23 (1827).

corporate work after a certain amount of the capital stock has been subscribed, such a charter provision is equivalent to an express authority to the corporation to call in the subscriptions as soon as this organization is affected.¹ Subscriptions to the full amount of the capital stock are held not to be necessary. The defense is not good.

§ 178. Where the subscription itself specifies how much of the capital stock must be subscribed before payment may be enforced, such specifications are legal and effective, and until they are fully complied with the subscriber is not liable.² A subscription of this kind is a conditional subscription.³ A condition that the subscription shall be payable only when sufficient subscriptions for the corporate purpose has been secured, has been held to require funds sufficient to put the enterprise in full operation.⁴ On the other hand, a subscription to pay "when required," renders the subscribers liable before the full capital stock is subscribed.⁵

§ 179. In England statutory provisions have almost entirely

¹ *Schenectady & S. P. R. Co. v. Thatcher*, 11 N. Y. 102 (1854); *Rensselaer & W. P. R. Co. v. Wetsel*, 21 Barb. 56 (1855); *Hamilton & D. P. R. Co. v. Rice*, 7 Barb. 166 (1849); *Sedalia, Warsaw, &c., Ry. Co. v. Abell*, 17 Mo. App. 645 (1885); *Hunt v. Kansas & M. B. Co.* 11 Kan. 412 (1873), the court saying that otherwise there would be no propriety in allowing the organization before the full capital was subscribed. *Hoagland v. Cin. & F. W. R. R. Co.*, 18 Ind. 452 (1862); *Hanover J. & S. R. R. Co. v. Haldeman*, 82 Pa. St. 36 (1876); *Penobscot & K. R. R. Co. v. Bartlett*, 12 Gray, 244 (1858), holding so, even though no contracts for building the road were to be made until a larger subscription was obtained. *Boston, B. & G. R. R. Co. v. Wellington*, 113 Mass. 79 (1873); *Minor v. Mechanics Bk.*, 1 Peters, 46; *New Haven & D. R. R. Co. v. Chapman*, 38 Conn. 65 (1871); *Illinois River R. R. Co. v. Zimmer*, 20 Ill. 654 (1858); *Lexington & W. C. R. R. Co. v. Chandler*, 54 Mass. 311; *Willamette F. Co. v. Stannus*, 4 Oreg. 261 (1872); *Jewett v. Valley Ry. Co.*, 34 O. St. 601 (1878). A vigorous case to the contrary is *Galveston Hotel Co. v. Balton*, 46 Tex. 633 (1877). The court says, "There were good reasons for

organizing the company to be found in the increased facility of thereby raising the subscriptions to the amount fixed for the capital stock and of other preliminary preparations for the execution of the work, when the subscription should reach that amount." A contrary rule "would render nugatory the most important provision of the charter, which is the amount of its capital stock." When the capital stock is to be fixed by the corporation, between two limits, the subscription of the full amount as fixed is a subscription of the full capital stock. *Kennebec & P. R. R. Co. v. Jarvis*, 34 Me. 360 (1852).

² Where by its terms, it is not to be binding until a certain amount is subscribed, it is enforceable when that amount is secured, although less than the full capital stock. *Bucksport & B. R. R. Co. v. Buck*, 65 Me. 536 (1876). See also *Iowa & Minn. R. R. Co. v. Perkins*, 28 Iowa, 281 (1869).

³ See Chap. V.

⁴ *People's Ferry Co. v. Balch*, 74 Mass. 203 (1857), the court holding that funds for the land, structures and boats, must be in hand before the defendant becomes liable.

⁵ *Cheraw & C. R. R. Co. v. Garland* 14 S. C. 63 (1880).

displaced the common-law rule. The principle that a subscriber is not liable until the full capital stock has been subscribed is recognized as having been the original rule at law. A few cases, however, seem to favor an opposite rule. Yet, an eminent English authority says that in all the cases in which the subscribers were held bound, they "had entered into a contract which precluded them from maintaining that the subscription of the whole of the originally proposed capital was an express or implied condition to their becoming shareholders." The English courts seem to have no clearly defined rule in this matter, but allow each case to turn largely on its own facts, releasing the subscriber if the discrepancy in the subscriptions is very large, and holding him liable if it is small, or if he in any way has aided the company in beginning business.¹

§ 180. Some difficulty has been experienced in determining what subscriptions shall be counted in ascertaining whether the full capital stock has been subscribed. Conditional subscriptions, the condition to which has not yet been performed by the corporation, are clearly not to be counted among the rest, since such

¹ *Norwich & L. Navigation v. Theobald*, 1 Moody & M. 151 (1828), required full subscription in accordance with a statute. *Fox v. Clifton*, 6 Bing. 776 (1830), the earliest common law English case on this subject, holds that the subscriber is not liable to corporate creditors unless the full capital stock has been subscribed. *Pitchford v. Davis*, 5 Mees. & W. 2 (1839), also fully agrees with the rule that prevails in this country. *Wontner v. Shairp*, 4 C. B. 404 (1847), sustained a recovery back of amounts paid on a subscription, under misrepresentations that the whole stock had been subscribed. *Waterford, W. W. & B. Ry. Co. v. Dalbiac*, 4 Eng. L. & Eq. 452 (1850), refused to allow the defense since the charter allowed the corporation to purchase land before the full capital stock was subscribed. *Watts v. Salter*, 10 C. B. 477 (1856), holds the same, the subscriber having aided in the incorporation, and given the directors power to proceed. *Galvanized Iron Co. v. Westoby*, 21 L. J. (Ex.) 302 (1852), per B. Parks, says, that at common law the subscriber is not liable unless the full capital stock is subscribed. *Johnston v. Goslett*, 3 C. B. N.

S. 569 (1857), makes the directors liable to the subscriber for his deposit when they so proceed. *London & C. Ins. Co. v. Redgrave*, 4 C. B. N. S. 524 (1858), holds the subscriber liable, he having aided in the incorporation. *Ornamental P. W. Co. v. Browne*, 2 Hurl. & C. 63 (1863), holds the subscriber liable, under the statute of 19 & 20 Vic. c. 47, similar to the American statutes. See also *McDougall v. Jersey I. H. Co.*, 10 Jur. N. S. 1043 (1864). *Peirce v. Jersey W. Co.*, L. R., 5 Ex. 209 (1870), required a certain amount to be subscribed, the charter itself so prescribing. *Elder v. New Zealand L. I. Co.*, 30 L. T. N. S. 285 (1875), the most important case on this subject, holds that where the directors are about to proceed with only one fourteenth of the capital stock subscribed, a subscriber may apply to the court and have his name removed from the subscribers' list. The court says that the case of *McDougall v. Jersey I. H. Co.*, *supra*, would have been decided otherwise had not two-thirds of the stock, in that case, been subscribed. See also *Howbeach Coal Co. v. Teague*, 5 H. & N. 151 (1860); *dictum* in *Re Jennings*, 1 Irish (Ch.), 654 (1851).

subscriptions may never become enforceable.¹ This rule, if strictly insisted upon, would probably occasion great inconvenience to the corporation in enforcing the subscriptions for stock.

The subscriptions of married women, infants, or persons of unsound mind, are to be excluded from the count.² So also the subscriptions of insolvents are excluded, unless at the time of subscribing they were apparently able to pay the subscription.³ Considerable difference of opinion exists as to whether subscriptions payable by their terms in labor, or materials, or contract work, are to be included in the count.⁴ The better rule seems to be that the necessity of employing this method of carrying out many modern corporate enterprises requires that such subscriptions should be counted, if the contract is made in good faith, and the contractors are reasonably responsible men.⁵ The weight of authority, however, holds otherwise. The records of the corporation are sufficient and competent evidence that the full capital stock has been subscribed.⁶

¹ *Troy & G. R. R. Co. v. Newton*, 74 Mass. 596 (1857), the condition being that the subscriber be allowed to pay in construction work. *Oskaloosa Agri. Works v. Parkhurst*, 54 Iowa, 357 (1880); *Cabot & W. S. B. v. Chapin*, 60 Mass. 50 (1850), where a subscription payable in other stock at par, when the market value was less, was not counted. *Ticonic Co. v. Lang*, 63 Me. 480 (1874). Subscription on condition that interest shall be paid is counted. *Rutland & B. R. R. Co. v. Thrall*, 35 Vt. 536 (1863). *Cf. Greenville & C. R. R. Co. v. Coleman*, 5 Rich. (S. C.) 118 (1851). Invalid subscriptions are not counted. *Belfast & M. L. R. R. Co. v. Cottrell*, 66 Me. 185 (1875). *Cf. Swartwout v. Mich. Air Line R. R. Co.*, 24 Mich. 389 (1872).

² *Phillips v. Covington & Cin. Bridge Co.*, 2 Metc. (Ky.), 219 (1859), holding that subscriptions of infants, married women, or insolvents, are not to be counted, unless already paid in. Fictitious paid up stock, and stock convertible into corporate bonds, counted. *Cf. Litchfield Bk. v. Church*, *supra*.

³ *Lewey's Island R. R. Co. v. Bolton*, 48 Me. 451 (1860); *Belfast, &c., Ry. Co. v. Inhab. of Brooks*, 60 Me. 568 (1872). The subsequent failure of some of the subscribers is immaterial. *Salem M. D. Corporation v. Ropes*, 23 Mass. 187 (1829).

⁴ Not counted where the contractor

failed to complete the work. *New York, H. & N. R. R. Co. v. Hunt*, 39 Conn. 75 (1872); *Troy & G. R. R. Co. v. Newton*, 74 Mass. 596 (1857), the court saying: "The receipt of the stock by them depended entirely upon a contingency, as the contractors might fail to do the work, and so no stock be earned;" *Oldtown & Lincoln R. R. Co. v. Veazie*, 39 Me. 571 (1855), where the contract work was not completed. In the case of *Ridgefield & N. Y. R. R. Co. v. Brush*, 43 Conn. 86 (1875), such subscriptions were counted, the contract for payment in work being parol, and not allowed to vary the apparently absolute subscription.

⁵ *Phillips v. Covington & Cin. Bridge Co.*, 2 Metc. (Ky.), 219 (1859).

⁶ *Penobscot R. R. Co. v. Dummer*, 40 Me. 172 (1855); *Id. v. White*, 41 Me. 512 (1856), unless proof be introduced to destroy their effect. A call is notice that the full amount has been subscribed. *Harlem Canal Co. v. Seixas*, 2 Hall (N. Y.), 504 (1829); *Id. v. Spear*, 2 Hall, 510; *Litchfield Bk. v. Church*, 29 Conn. 137 (1860), holding that the certificate of the commissioners that the full stock had been subscribed would not be questioned, even though they had counted married women's subscriptions. To same effect see *Lane v. Brainerd*, 30 Conn. 565 (1862); *Marlborough Branch R. R. Co. v. Arnold*, 9 Gray, 159 (1857). If the corporate records are

§ 181. A subscriber may waive the defense that the full capital stock of the corporation has not been subscribed. This waiver may be either express or implied from the acts or declarations of the subscriber.¹ Many different facts have been passed upon by the courts and held either to constitute or not to constitute a waiver of this defense. Thus it has been held to amount to a waiver for the subscriber to act as a director, attend meetings, and contract corporate debts;² or to pay assessments for several years, with full knowledge of all the facts;³ or to write to the directors, requiring them to call a meeting;⁴ or to participate as a stockholder and committeeman for several months;⁵ or to act as president of the corporation.⁶ But a subscriber does not waive this defense by paying a deposit;⁷ or by attending a meeting;⁸ or by participating in preliminary work and paying a statutory percentage required to be paid at the time of subscribing;⁹ or by paying assessments for surveys.¹⁰

§ 182. *Failure to fix definitely the capital stock, where the amount is left in the discretion of the corporation.*—Sometimes corporate charters, especially in the New England States, are granted without specifying the exact amount of the capital stock, but either fixing the outside limit or allowing the corporate authorities to fix it between certain specified limits. Where the charter leaves the amount of the capital stock indefinite, it is the duty of the proper corporate authorities to determine what it shall be, and no subscriber can be held liable on his subscription until such determination is made.¹¹ After the capital stock is once

destroyed or lost, there should be other clear evidence. *Central Turnpike Co. v. Valentine*, 10 Pick. 142 (1830).

¹ *Emmitt v. Springfield J. & P. R. R. Co.*, 31 Ohio St. 23 (1876); *Hager v. Cleveland*, 36 Md. 476 (1872).

² *Hager v. Cleveland*, *supra*.

³ *Morrison v. Dorsey*, 48 Md. 461 (1877).

⁴ *Tredwen v. Bourne*, 6 Mees. & W. 461 (1840), holding it to be evidence of waiver.

⁵ *Sharpley v. Louth & E. C. Ry. Co.*, L. R. 2 Ch. Div. 663 (1876).

⁶ *Corwith v. Culver*, 69 Ill. 502 (1873).

⁷ *Pitchford v. Davis*, 5 Mees. & W. 2 (1839).

⁸ *Wontner v. Shairp*, 4 C. B. 404 (1847); *New H. Central R. R. Co. v. Johnson*, 30 N. H. 390 (1855).

⁹ *Livesey v. Omaha Hotel*, 5 Neb. 50 (1876); *Oldtown & L. R. R. Co. v. Veazie*, 39 Me. 571 (1855), where as an officer the subscriber aided in preliminary work. This case goes farther and holds that there can be no waiver under any state of facts.

¹⁰ *Memphis Branch R. R. Co. v. Sullivan*, 57 Ga. 240 (1876); *Atlantic Cotton Mills v. Abbott*, 63 Mass. 423 (1852), holds that paying assessments and attempting to transfer is not a waiver. *May v. Memphis B. R. R. Co.*, 48 Ga. 109 (1873), holds that paying an assessment with notice of this defense is no waiver of it.

¹¹ *Worcester & N. R. R. Co. v. Hinds*, 62 Mass. 110 (1851); *Troy & G. R. R. Co. v. Newton*, 74 Mass. 596 (1857); *Pike v. Shore Line*, 68 Me. 445 (1878); *Somerset R. R. Co. v. Clarke*, 61 Me. 384 (1871). *Contra*, *Warwick R. R. Co. v. Cady*, 11 R.

fixed, there seems to be no rule preventing its being varied subsequently, provided the specified charter limits are observed.¹ It has been held that even subscriptions to the amount of the lowest limit allowed by the charter are insufficient, unless that limit has been designated by the corporate authorities as the amount of the capital stock.² After the capital stock is so determined, the full amount thereof must be subscribed before any subscriber is liable.³ It is not necessary that the amount of the capital stock be fixed by formal declaration of the corporate authorities. It may be done by acts equivalent thereto. Thus a resolution to close the books on a given day;⁴ or limiting the time of subscription and then closing the subscription books;⁵ or voting that a certain amount of stock in addition to existing subscriptions shall be issued,⁶ are the same as, and are equivalent to, an express resolution that the capital stock shall be the amount of subscriptions thus taken.

§ 183. *Irregular incorporation of the company.*—Under the laws of most of the States, charters of incorporation are obtained by complying with the provisions of what are called general incorporating acts. Usually these acts provide that a specified number of persons, by filing at a public registry a certificate setting out certain facts, may thereby form a corporation for the purposes named in such certificate. The various steps to be taken, and the contents of each certificate, are prescribed by the statute, and yet, frequently, in the formation of a corporation, under the statute, some part of the proceeding, through inadvertence or mistake, is not strictly complied with. The same thing happens, also, under acts incorporating a certain company, and requiring it to perform

¹ I. 131 (1875); *City Hotel v. Dickinson*, 72 Mass. 586 (1862). In the case of *Kirksey v. Florida & G. P. R. Co.*, 7 Fla. 23 (1857), it was held that the corporate charter need not mention any capital stock or shares of stock, and yet subscriptions may be taken and enforced. In the case of *Ward v. Griswoldville Mfg. Co.*, 16 Conn. 593 (1844), where the charter allowed the capital stock to vary from \$5,000 to \$50,000, it was assumed that the subscriptions were enforceable, although no fixed capital stock had been settled upon. In the case of *White Mts. R. R. Co. v. Eastman*, 34 N. H. 124 (1856), the charter allowed assessments when the

lower limit of the capital stock was reached.

² *Somerset & K. R. R. Co. v. Cushing*, 45 Me. 524 (1858); *Troy & G. R. R. Co. v. Newton*, 74 Mass. 596 (1857), *dicta*, however, in both of these cases.

³ *Pike v. Shore Line*, 68 Me. 445 (1878).

⁴ *Somerset & K. R. R. Co. v. Cushing*, 45 Me. 524 (1858).

⁵ *Lexington & W. C. R. R. Co. v. Chandler*, 54 Mass. 311 (1847).

⁶ *Bucksport & B. R. R. Co. v. Buck*, 65 Me. 536 (1876).

⁷ *Penobscot & K. R. R. Co. v. Bartlett*, 78 Mass. 244 (1858).

specified things, in order to render the incorporation complete. These defects undoubtedly render the corporate charter forfeitable at the instance of the State. Such defects in the process of becoming incorporated have also been the subject of some controversy as a defense to an action by the corporation to collect subscriptions to its stock.

§ 184. When an action is brought to collect a subscription, either directly or indirectly for the benefit of corporate creditors, it is well established that the subscribers cannot defeat such action by the defense that the corporation was not an incorporation by reason of its not having fully complied with the terms of the statute providing for such an incorporation.¹ Not only is the subscriber estopped, by the act of subscribing, from setting up this defense, but he is bound also by the rule that the existence of a corporation cannot be inquired into, except by a direct proceeding in behalf of the State. It is sufficient that the corporation exists *de facto*. If there is no authority of law for such a corporation, the members are liable as partners.

§ 185. As between the corporation itself and the subscribers there is difficulty and doubt in determining the rule. The great weight of authority lays down the broad rule that "where there is a corporation *de facto*, with no want of legislative power to its due and legal existence; where it is proceeding in the performance of corporate functions and the public are dealing with it on the supposition that it is what it professes to be; and the questions suggested are only whether there has been exact regularity and strict compliance with the provisions of the law relating to incorporations; it is plainly a dictate alike of justice

¹ *Hickling v. Wilson*, 104 Ill. 54 (1882); *Wheelock v. Kost*, 77 Ill. 296 (1875); *Upton v. Hansbrough*, 3 Biss. 317 (1873), the court saying: "I understand the rule to be well settled that where papers having color of compliance with the statutes, have been filed with the proper State officers and meet their approval, but are in fact so defective as to be incapable of supporting the corporation as against the State, they are, as against a subscriber to its capital, held sufficient to constitute a corporation *de facto*, if supported by proof of user." *Clark v. Thomas*, Rec. &c., 34 O. St. 46 (1874);

Voorhees v. Receiver of Bk. &c., 19 Ohio, 463 (1850); *Ossipee Co. v. Canney*, 54 N. H. 295 (1874); *Thompson v. Reno Sav. Bk.*, 7 Pac. Rep. 68 (Nev., 1885); says, "The certificate is made for the benefit of the public, not for the corporation or its stockholders. Those who participated in the incorporation of this bank, and, by a certificate made in pursuance of the statute, announced the amount of its capital stock, cannot as against the creditors of the corporation, contradict their own certificate." See also Chapter XIII.

and of public policy, that in controversy between the *de facto* corporation and those who have entered into contract relations with it, as corporators or otherwise, that such questions should not be suffered to be raised.”¹ This, doubtless, is the law of the

¹ Cooley, J., in *Swartwout v. Mich. Air Line R. R. Co.*, 24 Mich. 389 (1872). The leading case on this subject is *Tar River Nav. Co. v. Neal*, 3 Hawks (N. C.), 520 (1825), where the court says, that “even where it is shown that such charter has been granted upon a condition precedent and persons are found in the quiet possession and exercise of those corporate rights, as against all but the sovereign, the precedent condition shall be taken as performed.” In this case the subscriber had participated in corporate meetings. *Wilmington C. & R. R. Co. v. Thompson*, 7 Jones’ L. (N. C.) 387 (1860); *Brookville & G. T. Co. v. McCarty*, 8 Ind. 392 (1856), holding also that the subscriber cannot set up that the corporation had forfeited its charter for misuser and non-user. *Central A. & M. Ass. v. Alabama G. L. Ins. Co.*, 70 Ala. 120 (1881), where the court says: that “whoever contracts with a corporation, having a *de facto* existence, the reputation of a legal corporation, in the actual exercise of corporate powers, and franchises, is estopped from denying the legality of the existence of the corporation, or inquiring into irregularities attending its formation, to defeat the contract, or to avoid the liability he has voluntarily and deliberately incurred.” It also holds that a subsequent statute curing the defect is constitutional and effective. *Appleton Mut. Fire Ins. Co. v. Jesser*, 87 Mass. 446 (1862), the court saying that where “persons were found with the consent and under the authority of the designated corporators, and without objection on the part of the sovereign power, actually exercising the corporate powers, and claiming and using the franchise, they constituted a corporation *de facto*; and the lawlessness of their organization cannot be impeached collaterally in an action to recover an assessment.” *McCarthy v. Lavasche*, 89 Ill. 270 (1878), holding that the defense is not allowable, even though the statute creating the corporation be unconstitutional. See *St. Louis Ass. v. Hennessey*, 11 Mo. App. 555; *Slocum v. Prov. S. & G. P. Co.*, 10 R. I. 112 (1871); *McHose v. Wheeler*, 45 Pa. St. 32 (1863); *Tarbell v. Page*, 24 Ill. 48 (1860), where no certificate was filed; *Wallworth v.*

Brackett, 98 Mass. 98 (1867); *Hanover J. & S. R. R. Co. v. Haldeman*, 82 Pa. St. 36 (1876), holding that non-user rendering the charter forfeitable is no defense. *Rowland v. Meader Furniture Co.* 38 O. St. 269 (1882), holding that actual judgment of forfeiture is no defense; *Meadow v. Gray*, 30 Me., 547 (1849); *Danbury & N. R. R. Co. v. Wilson*, 22 Conn. 435 (1853), where the subscriber acted as a director; *Central P. R. Co. v. Clements*, 16 Mo. 359 (1852); *Maltby v. Northwestern Va. R. R. Co.* 16 Md. 422 (1860), where the subscriber had already paid calls; *Crawford R. R. Co. v. Lacey*, 3 Y. & J. 80 (1829), where incorporation was obtained by a false representation to Parliament; *Rockville & W. T. Co. v. Van Ness*, 2 Cranch C. C. 449 (1824), where the subscriber had taken part in an election; *Monroe v. Fort W. J. & S. R. R. Co.*, 28 Mich. 272 (1873), where only three instead of five signed the certificate. *Rice v. Rock I. & A. R. R. Co.*, 21 Ill. 93 (1859); *Hunt v. Kansas & M. Bridge Co.*, 11 Kan. 412 (1873), where the subscriber acted as director. *Ossipee H. & W. Mfg. Co. v. Canney*, 54 N. H. 295 (1874); *Home Stock Ins. Co. v. Sherwood*, 72 Mo. 460 (1880); *Gill v. Ky. & C. G. & S. Min. Co.*, 7 Bush, 635 (1870); *Wood v. Coosa & C. R. R. Co.*, 32 Ga. 273 (1861); *Hager v. Bassett*, 36 Md. 476 (1872); *East P. Hotel Co. v. West*, 13 La. Ann. 545 (1858). In New York the first case is *Dutchess Cotton Manufactory v. Davis*, 14 Johns. 238 (1817); *Schenectady & S. P. R. Co. v. Thatcher*, 11 N. Y., 102 (1854); *Eaton v. Aspinwall*, 19 N. Y. 119 (1859); *Methodist E. U. Ch. v. Pickett*, 19 N. Y. 482 (1859), the court saying it is sufficient for the corporation to be *de facto*. “Two things are necessary to be shown in order to establish the existence of a corporation *de facto*, viz.: (1) The existence of a charter, or some law under which a corporation with the powers assumed might lawfully be created; and (2) a user by the party to the suit, of the rights claimed to be conferred by such charter or law. The rule established by law as well as by reason is, that parties recognizing the existence of corporations by dealing with them have no right to object to any irregularity in

land, although a carefully considered case in Missouri allowed a subscriber, who had not done more than merely subscribe to set up this defense against the corporation, no creditor's rights being involved, and the court declared that all the cases denying the defense were cases where the subscriber had acquiesced "either by the payment of part of the subscription or by becoming a director, or by attending meetings of stockholders, or by any other act indicating an acquiescence in the validity of his subscription."¹

§ 186. There is another class of cases in which a subscriber for stock is allowed to make the defense that the corporation has not been regularly and legally incorporated. Where the subscriber made his contract of subscription previous to and in anticipation of the incorporation, and does not act subsequently, whereby he acquiesces in the mode of incorporation, he may set up that the corporation has not been incorporated and that he is not liable. The rule that a person contracting with a corporation recognizes thereby its capacity to contract and cannot afterwards deny it in that transaction, does not apply to one who subscribes before incorporation. He may insist upon the organization of a regular and legal corporation.²

their organization." *Black R. & U. R. R. Co. v. Clarke*, 25 N. Y. 208 (1832); *Leonardsville Bk. v. Willard*, 25 N. Y. 574 (1862); *Buffalo & Allegany R. R. Co. v. Cary*, 26 N. Y. 75 (1852); *Aspinwall v. Sacchi*, 57 N. Y. 331 (1874). Not, however, where at the time of signing the articles, the names of the directors, required to be inserted, were not inserted. *Dutchess & C. C. R. R. Co. v. Mabbett*, 58 N. Y. 397 (1874); *Cayuga Lake R. R. Co. v. Kyle*, 64 N. Y. 185 (1876); *Phoenix Warehousing Co. v. Badger*, 67 N. Y. 294 (1876); *De Witt v. Hastings*, 69 N. Y. 518 (1877), admitting the defense on the ground that there was no user of a corporate franchise. *Ruggles v. Brock*, 6 Hun, 164 (1875); *Mead v. Keeler*, 24 Barb. 20 (1857); *Abbott v. Aspinwall*, 26 Barb. 202 (1857); *Childs v. Smith*, 55 Barb. 45 (1869). This is also the rule in the Federal courts. *Webster v. Upton*, 91 U. S., 65 (1875); *Chubb v. Upton*, 95 U. S. 665 (1877). *Contra*, *Thompson v. Guion*, 5 Jones' Eq. (N. C.) 113 (1859).

Cf. Katama Land Co. v. Holly, 129 Mass. 540 (1880). The lapse of the charter, by limitation of time within which work must be commenced, is good defense. *McCully v. Pittsburgh & C. R. R. Co.*, 32 Pa. St. 25 (1858).

¹ *Kansas City Hotel Co. v. Hunt*, 57 Mo. 126 (1874).

² *Dorris v. Sweeney*, 60 N. Y. 463 (1875); *Rikhoff v. Browne*, R. S. S. M. Co., 68 Ind., 388 (1879); *Indianapolis F. & Min. Co. v. Herkimer*, 46 Ind. 142 (1874); *Nelson v. Blakey*, 47 Ind. 38 (1874); *McIntyre v. McLane D. Ass.* 40 Ind. 104 (1872); *Richmond Factory Ass. v. Clarke*, 61 Me. 351 (1873); *Reed v. Richmond Street R. R. Co.*, 50 Ind. 342 (1875); *Taggart v. Western Md. R. R. Co.*, 24 Md. 563 (1866), the court saying "The preponderance of authority in favor of a strict compliance with the provisions of the charter, in cases of subscriptions, prior to the organization of the company, is such as is not to be disregarded."

§ 187. *Ultra vires acts of the directors or the corporations.*—

A subscriber for stock in a corporation cannot defeat an action to collect such subscription by the defense that the directors or the corporation itself have done corporate acts which are beyond the corporate powers.¹ There are other remedies open to the subscriber. He may either impair such *ultra vires* acts, or may have them set aside if already accomplished.² This defense is clearly distinguishable from the common defense of amendments to the charter, by the fact that the acts here complained of have no sanction from the legislative authorities.³ Thus it has been held that a subscriber cannot defeat an action to collect his subscription by showing that the corporation has, without authority of law, and in excess of its powers, executed a lease or sale of the road;⁴ or illegally issued its bonds;⁵ or purchased shares of its own stock,⁶ or of another corporation;⁷ or changed the location or route of the road.⁸ The last instance especially, has been a frequent defense, but has been uniformly discountenanced by the courts whenever the change is made, not by an amendment to the

¹ First Municipality of N. O. v. Orleans Theatre Co., 2 Rob. (La.), 209 (1842); Hannibal R. C. & P. P. R. Co. v. Menifee, 25 Mo. 547 (1857); Vicksburg, S. & T. R. R. Co. v. McKean, 12 La. Ann. 638 (1857); Smith v. Tallahassee, &c., Plank Road Co., 30 Ala. 650 (1857); Prop. of City Hotel v. Dickinson, 72 Mass. 586 (1856); Court-right v. Deeds, 37 Iowa, 503 (1873); Ill. Grand T. R. R. Co. v. Cook, 29 Ill. 237 (1862); Hammett v. Little Rock & N. R. R. Co., 20 Ark. 204 (1859). In the case, however, of Macedon & B. P. R. Co. v. Lapham, 18 Barb. 315 (1854), an *ultra vires* extension of the line was held to be a good defense.

² "The stockholder has his remedy by injunction not to enjoin the collection of calls due upon his stock, but to restrain the corporation from the particular violation or abuse of its charter complained of." Miss., O. & Red R. R. Co. v. Cross, 20 Ark. 443 (1859). In *Ex parte* Booker, 18 Ark. 338 (1857), an application for an injunction to restrain the corporation from enforcing the payment of a subscription, on the ground that the corporation had committed *ultra vires* acts, was refused.

³ Caley v. Phil. & C. C. R. R. Co. 80 Pa. St. 363 (1876).

⁴ Hays v. Ottawa, O. & F. R. V. R. R. Co., 61 Ill. 422 (1871); Ottawa, O. & F. R. V. R. R. Co. v. Black, 79 Ill. 262 (1875); Chicago, B. & Q. R. R. Co. v. McGinnis, 79 Ill. 269 (1875); Ill. Mid. Ry. Co. v. Supervisors, &c., 85 Ill. 313 (1877); South Ga. & Fla. R. R. Co. v. Ayres, 56 Ga. 230 (1876); see also Tuttle v. Mich. Air-line R. Co., 35 Mich. 247; Troy & Rutland R. R. Co. v. Kerr, 17 Barb. 581 (1854). Or the whole of a business. Plate Glass Ins. Co. v. Sunley, 8 El. & Bl. 47 (1857).

⁵ Merrill v. Reaver, 50 Iowa, 404 (1879).

⁶ Re Republic Ins. Co., 3 Biss. 452 (1873.)

⁷ Cheltenham v. Republic Life Ins. Co., 86 Ill. 220 (1877).

⁸ Central P. R. Co. v. Clemens, 16 Mo. 359 (1852); Miss., O. & Red R. R. Co. v. Cross, 20 Ark. 443 (1859); Rives v. Montgomery, South P. R. Co. 30 Ala. 92 (1857). Where, however, the terminus was made 2,000 feet away from the location designated by charter, this fact was held to constitute *prima facie* a good defense. Chartiers R. R. Co. v. Hodgins, 77 Pa. St. 187.

charter, but by the arbitrary, unauthorized act of the corporate authorities.

§ 188. *Frauds and mismanagement of directors.*—This defense is very similar to the preceding one, and is governed by the same rules of law. A stockholder cannot defeat an action to collect his subscription by the defense that the corporate affairs have been managed fraudulently, or recklessly, or negligently.¹ The stockholder's remedy for such evils are of a different nature. For fraud, he may bring the guilty parties to an accounting.² For mismanagement, his only remedy is the corporate elections. In no case has he been allowed to escape liability on his subscription by reason thereof. Thus it is no defense that the corporate authorities fraudulently placed an overvaluation on property purchased by them for the corporation;³ nor that they have made a fraudulent contract with a construction company.⁴

§ 189. *Delay and abandonment of the enterprise.*—As a general rule it is no defense to an action on a subscription, to allege that the enterprise has been unduly delayed.⁵ This defense is frequently that there has been a non-user of the corporate franchises.⁶ It is, however, a well established principle that non-user of corporate franchises can be complained of only by the State, or in the name of the State. A subscriber has been held not to be discharged by the fact that the corporation was engaged thirteen years in completing its enterprise, a turnpike.⁷ Nor does a

¹ *People v. Barnett*, 91 Ill. 422 (1879); *Cheltenham v. Republic Life Ins. Co.*, 86 Ill. 220 (1877); *Merrill v. Reaver*, 50 Iowa, 404 (1879). Depreciation of the stock by reason of mismanagement, no defense. *People v. Barnett*, 91 Ill. 422 (1879).

² See Part IV. In the case *Hodgkinson v. Nat'l Live Stock Ins. Co.*, 26 Beav. 473 (1859), equity restrained the enforcement of calls already made, by reason of the fraud of the directors, but it was conceded in this case that the subscriber was still liable on his subscription.

³ *Hornaday v. Ind. & Ill. Central R. Co.*, 9 Ind. 263 (1857); *Dorris v. French*, 4 Hun, 292 (1875), where a patent right was purchased by the directors, from themselves for the corporation, at an exorbitant price.

⁴ *People v. Logan County*, 63 Ill. 374, 387 (1872).

⁵ *Pickering v. Templeton*, 2 Mo. App. 424 (1876); *Miller v. Pittsburgh & C. R.*

R. Co., 40 Pa. St. 237 (1861), where there was a delay of two and one half years, the court saying, "Until it can be shown how railroads can be built without money, no such defense as is here set up can prevail." *First Nat'l Bk. v. Hurford*, 29 Iowa, 579 (1870), where there was a delay in the performance of a condition subsequent to the subscription. See also *Union Hotel Co. v. Hurssee*, 79 N. Y. 454 (1880); rev'g 15 Hun, 371. *Boyle's Case*, 54 L. J. (Ch.) 550 (1885), holds that after a winding up has commenced there can be no withdrawal, but the court in a *dictum* clearly says that an unreasonable delay in organizing will authorize a withdrawal by the subscriber.

⁶ *Ouachita & Red R. R. Co. v. Cross*, 20 Ark. 443 (1855); *Hammett v. Little Rock & N. R. R. Co.* 20 Ark., 204 (1859).

⁷ *Gibson v. Columbia & N. R., T. & B. Co.* 18 O. St. 396 (1868).

temporary abandonment of the work release the subscriber.¹ But when the corporate work was not commenced for nine years, and, in the meantime, the subscriber had acted on the supposition of an abandonment and had sold property which the road was expected to benefit, he was held not liable on the subscription.² But an abandonment of part of the enterprise is no defense.³

A subscriber cannot defeat the subscription by the fact that the corporation has not completed, and has no intention of completing, the road in its entirety;⁴ nor by the fact that the road has been sold under foreclosure.⁵ In Pennsylvania, a failure on the part of the corporation to make a call for the subscription within six years, the statutory time of limitations on the collection of parol debts, is held to constitute an abandonment of the subscription and to be a good defense.⁶ If the corporation is insolvent, and the subscription is needed to pay corporate creditors, abandonment cannot be set up.⁷

§ 190. *Failure of the corporate enterprise.*—The entire failure of the enterprise, and the insolvency of the corporation is not a defense to an action on calls.⁸ This defense would seem on the face of it to be frivolous, and yet is occasionally set up. Under the American doctrine, a subscription is enforceable most of all, when it is needed to pay corporate creditors. This defense is closely allied to those that precede, and differs in little from the defense of abandonment of the enterprise.

§ 191. *Subscriptions of other subscribers released, or cancelled, or given on special terms.*—It is no defense for one subscriber, when sued upon his subscription, to allege that the sub-

¹ McMullen v. Maysville & Lex. R. R. Co. 15 B. Monr. (Ky.) 218 (1854).

² Fountain Ferry T. R. Co. v. Jewell, 8 B. Monr. (Ky.) 147 (1848).

³ Dorman v. Jacksonville & A. P. R. Co., 7 Fla. 265 (1857).

⁴ Buffalo & J. R. R. Co. v. Gifford, 87 N. Y. 294 (1882); aff'g 22 Hun, 359.

⁵ Id.

⁶ Pittsburgh & C. R. M. Co. v. Byers, 32 Pa. St. 22 (1858). The same rule is stated less broadly in McCully v. Pittsburgh, &c. J. R. R. Co., 32 Pa. St. 25 (1858), where the court says, "if the delay was not satisfactorily accounted for, subscribers would be at liberty after that lapse of time to consider the enterprise

abandoned." In this case an actual abandonment and return of subscription money to other subscribers was held to release all the subscribers.

⁷ Phoenix Warehousing Co. v. Badger, 67 N. Y. 294 (1876); Smith v. Gower, 2 Duv. (Ky.) 17 (1865); Hardy v. Merriweather, 18 Ind. 203, and see the following defense.

⁸ Bish v. Bradford, 17 Ind. 490 (1861); Morgan County v. Thomas, 76 Ill. 120, 141 (1875); Four Mile V. R. R. Co. v. Bailey, 18 O. St. 208 (1868). Assessments are collectible though the work is not completed. Red W. Hotel Co. v. Friedrich, 26 Minn. 112 (1879). See § 189, n. 5, *supra*.

scriptions of other subscribers have been cancelled, or that secret and more favorable terms were given to them than to him. If there has been a legal cancellation of other subscriptions the defendant cannot complain.¹ If he has the same right to a cancellation, he may obtain it by a suit for that purpose.² A secret agreement of the corporation with certain subscribers to stock, whereby they are to be released from payment, or to have some other advantage not common to all the subscribers, is no defense to a subscriber who was not promised the same advantages.³ All such secret agreements are void, and the subscribers receiving them are liable on their subscriptions absolutely as though no special advantages had been promised. Being so, a subscriber, though he did not participate therein, cannot complain. The fact that the corporation has forfeited the stock of other subscribers, and has compromised with still others, is no defense to a subscriber sued for calls.⁴ So also the failure of another subscriber to pay the percentage required by statute is not a defense.⁵

§ 192. *Failure of the corporation to tender a certificate.*—

It is no defense to an action on a subscription to allege that the corporation has not delivered nor tendered to the defendant the certificate of stock to which he is entitled.⁶ The certificate is

¹ *Rensselaer & W. P. R. Co. v. Wetzel*, 21 Barb. 56 (1855). If, however, the cancellation is on account of an abandonment of the enterprise, any other subscriber, when sued subsequently on his subscription, may set up such abandonment and cancellation, and thereby defeat the action. *McCully v. Pittsburgh & C. R. R. Co.*, 32 Pa. St. 25 (1858).

² *County of Crawford v. Pittsburgh & Erie R. R. Co.*, 32 Pa. St. 141 (1858).

³ *Anderson v. Newcastle & R. R. Co.*, 12 Ind. 376 (1859); *Jewett v. Valley Ry. Co.*, 34 O. St. 601; *Agri. C. Ins. Co. v. Fitzgerald*, 15 Jur. 489 (1859); *Memphis Branch R. R. Co. v. Sullivan*, 57 Ga. 240 (1876); *Hall v. Selma R. R. Co.*, 6 Ala. 74; *Conn. &c., R. R. Co. v. Bailey*, 24 Vt. 465; *Jewell v. Rock R. P. Co.*, 101 Ill. 57 (1881). In the case *Cleveland Iron Co. v. Ennor*, 4 Northeast Rep. 762 (Ill. 1886), the court said: "Such secret agreement was fraudulent as to the other subscribers, and was void and of no avail, and the subscription is to be regarded a valid one for the amount subscribed." See also *Thompson v. Reno Sav. Bk.*, 7 Pac. Rep. 68 (Nev., 1885). The sub-

scriber has the burden of proof that other subscriptions are colorable and fictitious. *Hayden v. Atlanta Cotton Factory*, 61 Ga. 233 (1878). The case of *Rutz v. Ester & R. Mfg. Co.*, 3 Bradw. (Ill.) 83 (1878), is contrary to the general rule. The case of *New York Exchange Co. v. De Wolf*, 31 N. Y. 270 (1865), reversing 5 Bosw. 593, holds that a subscriber may defeat an action on his subscription by showing that other subscriptions were unauthorized, and not enforceable. See also *Berry & Yates*, 24 Barb. 199; *Nickerson v. English*, 6 East. Rep. 651 (Mass., 1886).

⁴ *Dorman v. Jacksonville & A. P. R. Co.*, 7 Fla. 265 (1857).

⁵ *Swartwout v. Mich. Air Line R. R. Co.*, 24 Mich. 389 (1872).

⁶ *Burr v. Wilcox*, 22 N. Y. 551 (1860), aff'g 6 Bos. 198; *Chandler v. Northern Cross R. R. Co.*, 18 Ill. 190 (1856); *Miller v. Wild Cat G. R. Co.*, 52 Ind. 51 (1875); *New Albany & S. R. R. Co. v. McCormick*, 10 Ind. 499 (1858); *Heaton v. Cincinnati & Ft. W. R. R. Co.*, 16 Ind. 275 (1861); *Kennebec &c., R. R. Co. v. Jarvis*, 34 Me. 360; *Chaffin v. Cummings*,

merely the stockholder's evidence of title to his stock. It is not the stock itself, but only a convenient representation of it. He would be a full stockholder with all the rights of one, if the certificate were never issued at all.¹ Consequently, since it is for him to demand the certificate when he wishes it, and not for the corporation to tender it, it is no defense for him to allege that he has never received the paper representative of his stock. The corporation must, however, be in a position to issue such certificate.² If certificates for the whole capital stock have already been issued, the defendant subscriber, by this fact, may defeat the action on his subscription.³ It has also been held that the plaintiff corporation must aver a readiness and willingness to deliver the certificate of stock.⁴

§ 193. *Set-off and counterclaim.*—It seems to be well established that, when a corporation has become insolvent, and the subscriptions for stock are being enforced for the benefit of corporate creditors, a subscriber cannot, in the suit brought to collect his subscription, set up a counterclaim or set-off.⁵ This rule is

37 Me. 76 (1853). The subscriber may stipulate otherwise in his subscription. *Summers v. Sleath*, 45 Ind. 598 (1874); *Schaeffer v. Mo. Home Ins. Co.*, 46 Mo. 248 (1870); *South Ga. & Fla. R. R. Co. v. Ayers*, 56 Ga. 234 (1876); *Vawter v. Ohio & Miss. R. R. Co.*, 14 Ind. 174 (1860); *Spear v. Crawford*, 14 Wend. 20 (1835); *Chester Glass Co. v. Dewey*, 16 Mass. 94 (1819); *Fulgum v. Macon & B. R. R. Co.*, 44 Ga. 597 (1872); *Minnesota Harvester Works v. Libby*, 24 Minn. 327 (1877); *Blyth's Case*, L. R., 4 Ch. Div. 140 (1876); *Agricultural Bk. v. Burr*, 24 Me. 256 (1844); *Hawley v. Upton*, 102 U. S. 314 (1880); *Wheeler v. Millar*, 90 N. Y. 353 (1882), aff'g 24 Hun, 541. The case of *Clark v. Continental Imp. Co.*, 57 Ind. 135 (1877), holds that where the action is for the whole subscription or the last instalments, a tender of the certificate, on condition of payment, is necessary. *St. Paul, &c., R. R. Co. v. Robbins*, 23 Minn. 440 (1877), holds that a tender is necessary where the issue is of preferred stock, after the whole original capital stock has been issued.

¹ *Fulgum v. Macon & Brunswick R. R. Co.*, 44 Ga. 597 (1872).

² *McCord v. Ohio & Miss. R. R. Co.*, 13 Ind. 220 (1859).

³ *Burrows v. Smith*, 10 N. Y. 550 (1853).

⁴ *James v. Cincinnati, H. & D. R. R. Co.*, 2 Disney, 261 (1858).

⁵ *Sawyer v. Hoag*, 17 Wall. 610 (1873); *Government S. Ins. Co. v. Dempsey*, 50 L. J. (Q. B.) 199 (1881). The leading case in England on this subject is *Grisell's Case*, L. R., 1 Ch. 528 (1866), where the court says, "if a set-off were attained against a call, it would have the effect of withdrawing altogether from the creditor's part of the funds, applicable to the payment of debts." See also *Black's Case*, L. R., 8 Ch. 254 (1872); *Mudford's Case*, L. R., 14 Ch. D. 634 (1880), spoken of in *Government S. I. Co. v. Dempsey*, *supra*, as holding that no counterclaim is to be allowed. *Gill's Case*, L. R., 12 Ch. Div. 755 (1879); *Calisher's Case*, L. R., 5 Eq. 214 (1868); *Barnett's Case*, L. R. 19 Eq. 449 (1875); *Re Whitehouse & Co.*, L. R., 9 Ch. Div. 595 (1878), disapproving *Brighton Arcade Co. v. Dowling*, L. R., 3 C. P. 175. See also *Matthews v. Albert*, 24 Md. 527 (1866); *Garnett & M. G. Min. Co. v. Sutton*, 3 B. & S. 321, allowing set-off was based on a statute repealed by Companies Act, 1862. See *Hillier v. Allegheny Mutual Ins. Co.*, 3 Pa. St. 470 (1846); *Long v. Penn. Ins. Co.*, 6 Pa. St. 421 (1847). Cf. *Scammon*

founded in equity and wise public policy. The stockholder is not deprived of his remedy for the debt due him from the corporation, but he is obliged to proceed in the same manner, and to participate in the final corporate assets and to the same extent, and at the same time, as other creditors.¹ Such is clearly the rule in New York.² Where, however, payment of a subscription is demanded or enforced for the benefit of the corporation itself, and not for corporate creditors, it is competent for the subscriber to set up, in defense to the action, a set-off or counterclaim.³

§ 194. There has been some question where a subscriber has voluntarily, and without the compulsion, request, or medium of the corporation, paid corporate creditors, whether he may claim that to the extent of such payments he has discharged his liability on his stock. It seems to be generally conceded that such an equitable set-off is allowed, both at law and in equity.⁴ Such a

v. Kimball, 92 U. S. 362 (1875). In *Seovill v. Thayer*, 105 U. S. 143, 152 (1881), the court says: "It is a general rule that a holder of claims against an insolvent corporation, cannot set them off against his liability for an assessment on his stock in the corporation, in a suit by an assignee in bankruptcy." To same effect *Thebus v. Smiley*, 110 Ill. 316 (1884); *Williams v. Traphagen*, 38 N. J. Eq. 57 (1884).

¹ *Grissell's Case*, *supra*. Cf. *Lang v. Penn. Ins. Co.*, *supra*.

² *Re Empire City Bank*, 18 N. Y. 199, 227 (1858), the court saying, "there is no reason why a creditor should be in any better situation on account of being at the same time a stockholder. . . . As a creditor he is entitled only to a dividend in proportion to the other creditors. In case of a deficiency in means to pay all the debts, he must take his dividend *pro rata*. But if he could set-off his claim as a creditor against his liability as a stockholder, he might be paid in full, while the other creditors would receive only part of the amount due them." See also *Osgood v. Ogden*, 4 Keyes, 70 (1868); *Lawrence v. Nelson*, 21 N. Y. 157 (1860). *Contra*, *Tallmadge v. Fishkill Iron Co.*, 4 Barb. 382 (1848). In the case *Wheeler v. Millar*, 90 N. Y. 353 (1882), the stockholder's subscription and statutory liability combined were sufficient to pay his own and the other debts involved in the case.

³ *Barnett's Case*, L. R., 19 Eq. 449 (1875). The set-off may be allowed by mutual agreement, and if free from fraud, it cannot be impeached upon the subsequent insolvency of the corporation. *Goodwin v. McGehee*, 15 Ala. (N. S.) 232 (1849). In *McLaren v. Pennington*, 1 Paige Ch. 102 (1828), it was held, that upon the repeal of a charter, the subscriber sued on his subscription might set-off every demand which he had against the corporation at the time of the repeal, but not demands which he afterwards purchased. See also *Paine v. Central Vt. R. R. Co.*, 118 U. S. 152 (1886).

⁴ In New York particularly, this rule has been applied and upheld. See *Briggs v. Penniman*, 8 Cowen, 387 (1826); *Garrison v. Howe*, 17 N. Y. 458 (1858), the court saying: "A stockholder may be absolutely discharged from all liability under this statute by payment, on legal compulsion, to any creditor or creditors for whose debts he is liable, if such payment equals the amount of his stock. . . . Probably the same effect would result from a voluntary payment." *Agate v. Sands*, 73 N. Y. 620 (1878). See also *Sackett's Harbor R. R. Co. v. Blake*, 2 Rich. Eq. 225 (1851); *Grose v. Hilt*, 36 Me. 22 (1853); *Whitman v. Porter*, 107 Mass. 522 (1871), a joint-stock company case. *Poole's Case*, L. R. 9 Ch. Div. 322. Cf. *Eastman v. Crosby*, 90 Mass. 206 (1864).

set-off differs from the ordinary set-off, in that no advantage was expected or received by the stockholder so paying, but his loss or payments on his stock are as great as though he had paid directly to the corporation itself. Such payments are frequently made in discharge of a liability imposed by statute on stockholders in addition to the subscription liability.¹

§ 195. *Statute of limitations.*—After a call has been made, and the subscription or a part of the subscription is thereby rendered due and payable, the Statute of Limitations begins to run. Difficulty, however, arises in determining whether the Statute begins to run before the call is made. In Pennsylvania there is an inclination to hold that the call must be made before six years have elapsed after the call is possible; otherwise the right to collection is barred.² But the better rule, and the one supported by the weight of authority, is that the Statute of Limitations begins to run on a subscription for stock only after a call has been made and is due.³ Where the statute is a bar against the corporation, it is a bar against corporate creditors.⁴ Courts of equity will generally apply the same period of limitation, unless there be special and equitable reasons for doing otherwise.⁵ Where a

¹ See preceding note.

² *McCully v. Pittsburgh & C. R. R. Co.*, 32 Pa. St. 25; *Pittsburgh & C. R. R. Co. v. Byers*, 32 Id. 22; *Id. v. Graham*, 36 Id. 77 (1859). *Cf. Id. v. Plummer*, 37 Id. 413 (1860).

³ *Taggart v. Western Md. R. R. Co.*, 24 Md. 563 (1866); *Western R. R. Co. v. Avery*, 64 N. C. 489 (1870); *Glenn v. Williams*, 60 Md. 93 (1882); *Baltimore, &c., Turnpike Co. v. Barnes*, 6 H. & J. (Md.) 57 (1823); *Salisbury v. Black's Admr.*, Id. 293; *Curry v. Woodward*, 53 Ala. 376 (1875), where the court says: "We presume no one of the stockholders imagined that if the business was prosperous, so that for six, eight, or ten years instead of having to pay this money in, they were receiving dividends from the income, and if afterwards, in consequence of losses, . . . it became necessary to pay . . . he could set up the Statute of Limitations in opposition to a call to pay in his stock."

⁴ *Stephen v. Ware*, 45 Cal. 110 (1872); *Davidson v. Rankin*, 34 Cal. 503 (1868), in probate matters. *Thompson v. Reno Sav. Bk.*, 7 Pac. Rep. 871 (Nev., 1885); *South Car. Mfg. Co. v. Bk. of S. C.*, 6 Rich.

Eq. (S. C.) 227 (1854). The statute applicable to written contracts applies, although the subscription is partly in writing. *Falmouth, &c., Co. v. Shawhan*, 5 North East. Rep. 408 (Ind., 1886).

⁵ *Bk. of U. S. v. Dallam*, 4 Dana (Ky.), 574 (1836). In the cases, however, of *Payne v. Ballard*, 23 Miss. 88 (1851), and *Hightower v. Thornton*, 8 Ga. 486 (1850), it was held that the Statute of Limitations had no application by analogy to the equitable actions to collect subscriptions. In *Terry v. Bk. of Cape Fear*, 20 Fed. Rep. 777 (1884), the court said in a similar case: "In adjusting equitable rights, courts of equity will never allow the Statute of Limitations to have a manifestly inequitable and unjust operation." In *Scovill v. Thayer*, 105 U. S. 143, 155 (1881), a case in equity, the court says: "Before there is any obligation upon the stockholder to pay without an assessment and call by the company, there must be some order of a court of competent jurisdiction, or, at the very least, some authorized demand upon him for payment. And it is clear the Statute of Limitations does not begin to run in his favor until such order or demand," citing cases.

subscriber defeats even a part of the action on his subscription, by setting up the Statute of Limitations, he cannot claim the stock, at least unless he pays the part which was barred by the statute.¹

§ 196. *Ignorance or mistake.*—It is no defense to an action for a subscription that the subscriber at the time of subscribing was ignorant of the actual condition of the corporation.² Nor is it a defense that he was ignorant of the legal effect of the subscription contract which he signs.³

§ 197. *Miscellaneous defenses.*—A subscriber cannot defeat an action for the collection of his subscription by alleging that the charter was obtained in bad faith;⁴ or that where a corporate creditor is enforcing payment, that such creditor is also a director of the corporation;⁵ or that other subscribers have paid their subscriptions in Confederate money;⁶ or that he has paid the subscription by note instead of by cash, as required by the charter;⁷ or that an illegal by-law prevents his voting until calls are paid;⁸ or that, by the charter, the whole capital stock should have been paid in before the commencement of business, which was not done;⁹ or that the corporation has been ousted from its franchises.¹⁰ A material alteration, however, in a subscription contract is a good defense, unless the corporation proves it to have been made without its knowledge or procurement.¹¹ The defense that the corporate charter has been amended by the legislature without the consent of the defendant subscriber, is considered elsewhere.¹²

¹ Johnson v. Albany & Susquehanna R. R. Co., 54 N. Y. 416, 426 (1873), where the court says: "The claim of the plaintiff is not supported by any principle that should give it any consideration in either a court of law or equity. The Statute of Limitations never paid a debt, although it barred a remedy."

² Payson v. Withers, 5 Biss. 269 (1873).

³ New Albany & S. R. R. Co. v. Fields, 10 Ind. 187 (1858); Clear v. Newcastle & D. R. R. Co., 9 Ind. 488 (1857). See also cases in Ch. IX, § 146.

⁴ Peychaud v. Love, 24 La. Ann. 404 (1872); Garrett v. Dillsburg & M. R. R. Co., 78 Pa. St. 465 (1875); Smith v. Heindecker, 39 Mo. 157 (1866).

⁵ Chouteau Ins. Co. v. Floyd, 74 Mo. 286.

⁶ Macon & Augusta R. R. Co. v. Vason, 57 Ga. 314 (1876).

⁷ Little v. O'Brien, 9 Mass. 423 (1812).

⁸ Chandler v. Northern Cross R. R. Co., 18 Ill. 190 (1856).

⁹ McDermott v. Dongan, 44 Mo. 85 (1869).

¹⁰ Gaff v. Flesher, 33 O. St. 107; Rowland v. Meader Furniture Co., 38 O. St. 269 (1882).

¹¹ Bery v. Marietta, &c., R. R. Co., 26 O. St. 673 (1875). Cf. Ellison v. Mobile & O. R. R. Co., 36 Miss. 572 (1858).

¹² See Chapter on Amendments of Charter.

§ 198. *Waiver of defenses.*—A subscriber to stock in a corporation may waive any defense he may have to the subscription. The waiver may be express, or it may arise by implication from the acts and declarations of the subscriber. Thus a payment of a call, with full knowledge of the defense, is held to be a waiver;¹ and any act indicating a clear intent to abide by, or accept, or pass over an objection which the subscriber might make, will be held to be a waiver.²

¹ *Miss. & Tenn. R. R. Co. v. Harris*, 36 Miss. 17 (1858); *Inter. Mountain P. Co. v. Jack*, 6 Pac. Rep. 20 (Montana, 1885); *Hamilton v. Grangers' Life & H. Ins. Co.*, 67 Ga. 145 (1881).

² See *May v. Memphis Branch R. R. Co.*, 48 Ga. 109 (1873); *Middlesex Turnpike Co. v. Seman*, 10 Mass. 385 (1813); *McCully v. Pittsburgh & C. R. R. Co.*, 32 Pa. St. 25 (1858).

CHAPTER XI.

THE STOCKHOLDERS' LIABILITY TO CORPORATE CREDITORS UPON UNPAID SUBSCRIPTIONS.

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| <p>§ 199. Unpaid subscriptions a trust fund for the benefit of creditors.</p> <p>200. Can be reached only after judgment against the corporation, and execution returned unsatisfied.</p> <p>201. The remedy by garnishment or attachment.</p> <p>202. The remedy by mandamus.</p> <p>203. The remedy by action at law.</p> <p>204. The remedy by bill in equity.</p> <p>205-206. Parties to the bill in equity.</p> <p>207. A court of equity may make a call.</p> | <p>§ 208. Receivers and assignees in bankruptcy or for the benefit of creditors. Their duties, powers, and liabilities as to shares not paid up.</p> <p>209. The judgment against the corporation impeachable only for fraud, or want of jurisdiction.</p> <p>210. Defenses in actions to compel payment of balances of subscriptions available against corporate creditors.</p> <p>211. Contribution.</p> |
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§ 199. *Unpaid subscriptions a trust fund for the benefit of creditors.*—The capital, or capital stock of a corporation, is the aggregate of the par value of all the shares into which the capital is divided upon the incorporation; it is the fund, or resource with which the corporation is enabled to act and transact its business, and upon the faith of which persons give credit to the corporation and become corporate creditors. The public, in dealing with a corporation, has the right to assume that its actual capital, in money or money's worth, is equal to the capital stock which it purports to have, unless it has been impaired by business losses. The public has a right also to assume that the capital stock has been or will be fully paid up, if it be necessary, in order to meet corporate liabilities. Accordingly, the American courts go very far to protect corporate creditors, and in this country it is a well settled doctrine that capital stock, and especially unpaid subscriptions to the capital stock, constitute a trust fund for the benefit of the creditors of the corporation.¹ There are three methods by which

¹ "Though it be a doctrine of modern date," says Mr. Justice Miller in *Sawyer v. Hoag*, 17 Wall. 610, 620 (1873), "we think it now well established that the capital stock of a corporation, especially its unpaid subscriptions, is a trust fund for

the benefit of the general creditors of the corporation. And when we consider the rapid development of corporations as instrumentalities of the commercial and business world in the last few years, with the corresponding necessity of adapting

stockholders seek to avoid their liability to corporate creditors: first, by a cancellation or withdrawal from the contract;¹ second, by a release from their obligation to pay the full par value of the stock;² third, by a transfer of the stock.³ In each of these cases, however, a court of equity does its utmost to protect the corporate creditors, and a rigid scrutiny will be made in the interest of creditors into every transaction of such a nature.⁴

legal principles to the new and varying exigencies of this business, it is no solid objection to such a principle that it is modern, for the occasion for it could not sooner have arisen." This seems to be a distinctively American doctrine. It is not known to the English law, and was first announced by Mr. Justice Story in *Wood v. Dummer*, 3 Mason, 308 (1824). See also the cases *Hightower v. Thornton*, 8 Ga. 486 (by Lumpkin, J.); *Barry v. Merchants' Exchange Co.*, 1 Sandf. Chan. 280; *Germantown, &c., Ry. Co. v. Fidler*, 60 Penn. St. 124 (1869); *Crawford v. Rohrer*, 59 Md. 599 (1882); *Lewis v. Robertson*, 21 Miss. 558 (1850); *Burke v. Smith*, 16 Wall. 390 (1872); *New Albany v. Burke*, 11 Id. 96 (1870); *Bunn's Appeal*, 105 Penn. St. 49 (1884); *Curran v. Arkansas*, 15 How. 304 (1853); *Ogilvie v. Knox Ins. Co.*, 22 Id. 380 (1859); *Mumma v. Potomac Co.*, 8 Peters, 281 (1834); *Payson v. Stoever*, 2 Dillon, 427 (1873); *Saenger v. Upton*, 91 U. S. 56 (1875); *Webster v. Upton*, 91 Id. 65 (1875); *Chubb v. Upton*, 95 Id. 665 (1877); *County of Morgan v. Allen*, 103 Id. 498 (1880); *Bassett v. St. Albans Hotel Co.*, 47 Vt. 313 (1875); *Tarbell v. Page*, 24 Ill. 46 (1860); *Osgood v. Laytin*, 3 Keyes (N. Y.), 521; s. c. 5 Abb. N. S. 1; *De Peyster v. American Fire Ins. Co.*, 6 Paige, 486 (1837); *Morgan v. New York, &c., R. R. Co.*, 10 Id. 290 (1843); *Thompson's Liability of Stockholders*, § 10. *Cf. Vose v. Grant*, 15 Mass. 505 (1819); *Spear v. Grant*, 16 Id. 9 (1819); *Baker v. Atlas Bank*, 9 Metc. 182 (1845); *Briggs v. Penniman*, 8 Cowen, 387 (1826); *Ex parte Jeaffreson*, L. R. 11 Eq. 115 (1870); *Spackman v. Evans*, L. R. 3 H. of L. 198 (1868); *Osgood v. King*, 42 Iowa, 478 (1876); *Chisholm v. Forny*, 65 Id. 333; *Jackson v. Traer*, 64 Id. 469. In New York, many decisions to this point have been rendered, especially in actions under the general Manufacturing Act (§ 10, Chap. 40, Laws of 1848). They are fully cited and considered in the chapter, *infra*, on Statutory Liability, *q. v.* See *Gillet v. Moody*, 5 Barb. 189 (1849);

Mills v. Stewart, 41 N. Y. 389 (1869); *Morgan v. New York, &c., R. R. Co.*, 10 Paige Chan. 290 (1843). To the same effect, see *Dr. Salmon v. The Hamborough Company*, 1 Cases in Chan. 204; *Temp. Car. II. Cf. 1 Foubl. Eq. 297n.* Proceedings between the King and the City of London, 8 Howell St. Tr. 1087; *Nevitt v. Bank of Port Gibson*, 6 Smed. & M. 513; *Hume v. The Winyaw & Wando Canal Co.*, 1 Carolina L. J. (by Desaussure, Chan.).

¹ See Chapter X.

² Id., also Chapter III.

³ See Chapter XV.

⁴ *Sawyer v. Hoag*, 17 Wall. 610 (1873); *County of Morgan v. Allen*, 103 U. S. 498 (1880); *Chouteau v. Dean*, 7 Mo. App. 211 (1879); *Gill v. Balis*, 72 Mo. 424; *Putnam v. City of New Albany*, 4 Biss. 365 (1869); *Re South Mountain, &c., Mining Co.*, 7 Sawyer, 30 (1881); *Union Ins. Co. v. Frear Stone Manfg. Co.*, 97 Ill. 537 (1881); *Singer v. Given*, 61 Iowa, 93 (1883); *Jackson v. Traer*, 64 Iowa, 469 (1884). In one case, it is said that it is not within the ingenuity of man to devise a scheme to prevent courts of equity from enforcing the payment of unpaid subscriptions to capital stock for the benefit of corporate creditors. *Upton v. Hansbrough*, 3 Biss. 417, 425 (1873). *Cf. Chisholm v. Forny*, 65 Iowa, 333 (1884). Unfortunately this cannot be said to be always the result of corporate creditors' suits to enforce such liability. Generally, however, the courts are able to give relief. Thus an arrangement entered into between the corporation and its stockholders, for the purpose of defeating the claims of creditors, in pursuance of which the stockholders are allowed, after it is ascertained that the corporation is insolvent, to buy in depreciated and repudiated claims against the company, and thus to extinguish their indebtedness for stock subscribed, is held fraudulent and void. *Goodwin v. McGehee*, 15 Ala. 232 (1849); *Thompson v. Meisser*, 108 Ill. 359 (1884). And a payment in full for stock, followed by an immediate loan of part or all of the

§ 200. *Can be reached only after judgment against the corporation, and execution returned unsatisfied.*—Although it may be considered settled law, at least in the United States, that unpaid subscriptions to the capital stock of corporations constitute a trust fund for the benefit of corporate creditors, yet such unpaid balances of subscription are not the primary or regular fund for the payment of corporate debts. Persons transacting business with the corporation look to the corporation itself for the payment of their debts. Credit is given to the corporation, not to the stockholders, and it is the natural order of business that the creditors of the corporation are to be paid by the corporation from funds in the corporate treasury. Ordinarily corporate creditors have no knowledge or concern about the subscription list, and unpaid or partially paid subscriptions are a matter entirely between the corporation and the subscribers. As long as the corporation meets its obligations in the ordinary course of business, corporate creditors have no need to concern themselves about unpaid subscriptions to the stock. But whenever the corporation is in default and embarrassed, or for any reason fails to pay its debts, then its creditors have rights with reference to such unpaid sub-

purchase-price by the corporation back to the subscriber, is a fraud as to creditors and the public, and will be set aside. *Sawyer v. Hoag*, 17 Wall. 610 (1873). See *Thomp. on Liability of Stock*, § 394. The stockholders' liability in this respect is not confined in general to the original capital stock, but it attaches upon an authorized increase of the capital, to such increase. *Chubb v. Upton*, 95 U. S. 665 (1877). See also *Weaver v. Mudgett*, 95 N. Y. 295 (1884); *Pacific National Bank Cases* (Supm. Ct. U. S., November 1886). The filing of the statutory certificate declaring that the whole amount of the capital stock has been paid in, is not conclusive of the fact, and will not prevent proof to the contrary. *Barre National Bank v. Hingham Manfg. Co.*, 127 Mass. 563 (1879); *Wheeler v. Millar*, 90 N. Y. 358 (1882); *Veeder v. Mudgett*, 95 Id. 295 (1884); *Thompson v. Reno Savings Bank*, 7 Pac. Rep. 68 (Nev. 1885). It has been held to be competent for any one dealing with the company to contract to hold the shareholders responsible to only a limited extent, to no extent at all, or to any specified extent mutually agreed.

Shelford on Joint Stock Companies (2d London edition), 4; 1 Lindley on Part. 377. Cf. *In re Athenæum Life Assurance Society*, 4 K. & J. 517 (1858); s. c. 3 De G. & J. 660; 27 L. J. Chan. 798; *In re State Fire Insurance Co.*, 1 Hem. & M. 457 (1863); s. c. 1 De G., J. & S. 634; 35 L. J. Chan. 834; 34 Id. 436; *Halkett v. Merchant Traders' Association*, 13 Q. B. 960 (1849); s. c. 29 L. J. Q. B. 59; *Hasell v. Merchant Traders' Association*, 4 Exch. 525; *Evans v. Coventry*, 3 Drew. 75 (1854); s. c. 5 De G., M. & G. 911; 8 Id. 835; 25 L. J. Chan. 834; *Lord Talbot's Case*, 5 De G. & Sm. 386 (1852); s. c. 21 L. J. Chan. 846. See also *Reid v. Allan*, 4 Exch. 326 (1849); s. c. 19 L. J. Exch. 39; *Addison v. Mayor of Preston*, 12 C. B. 108, and compare *In re Independent Assurance Co.*; *Ex parte Cope*, 1 Sim. (N. S.) 54; *Sunderland Marine Insurance Co. v. Kearney*, 16 Q. B. 925 (1851); s. c. 20 L. J. (Q. B.) 417; *Pedell v. Gwynn*, 1 Hurl. & N. 590 (1857); s. c. 26 L. J. Exch. 199; *Gordon v. Sea, Fire and Life Assurance Society*, 1 Hurl. & N. 599 (1857); s. c. 29 L. J. Exch. 202, and see *Hess v. Werts*, 4 Sarg. & R. 361 (1818).

scriptions. They then have the right to know whether all the subscriptions for stock have been fully paid in, and if not, they have the right to compel such a payment.

It accordingly becomes important to know at what point in their efforts to collect what is due them, corporate creditors may cease to pursue the corporation and proceed directly against its delinquent members. The well established rule upon this point is that a corporate creditor's suit, to enforce payment of unpaid subscriptions, can be properly brought only after a judgment at law has been obtained against the corporation, and an execution returned unsatisfied.¹ This rule is of such importance that, by statute, in many of the States, a creditor's right to proceed against a stockholder on his unpaid subscription is allowed only after the remedy against the corporation itself has been exhausted.² By this is meant that judgment shall have been duly recovered against the corporation, and execution issued and regularly returned unsatisfied. Nothing short of that exhausts the remedy against the corporation.³

¹ *Bank of the United States v. Dallam*, 4 Dana, 574 (1836); *Walser v. Seligman*, 21 Blatchf. 130 (1882); *Wetherbee v. Baker*, 35 N. J. Eq. 501 (1882); *Cutright v. Stanford*, 81 Ill. 240 (1876); *Baxter v. Moses*, Me. (1885); *Munger v. Jacobson*, 99 Ill. 349 (1881); *Terry v. Anderson*, 95 U. S. 636 (1877); *Cleveland v. Burnham*, 55 Wis. 598 (1885); *Freeland v. McCullough*, 1 Denio, 414 (1845). The bill can usually be filed for this purpose only in the courts of the State where the corporation exists. *Barclay v. Tallman*, 4 Edw. Chan. 128 (1842); *Murray v. Vanderbilt*, 39 Barb. 147; *Bank of Virginia v. Adams*, 1 Pars. Eq. 534 (1850); *Patterson v. Lynde*, 112 Ill. 196 (1884); *Harris v. Pullman*, 84 Id. 25 (1876). Cf. *Claffin v. McDermott*, 12 Fed. Rep. 375 (1882); *McLune v. Benceni*, 2 Ired. Eq. 513; *Farned v. Harris*, 19 Miss. 366 (1848); *Bullitt v. Taylor*, 34 Id. 708 (1858); *Verplanck v. Ins. Co.*, 6 Paige, 503; *Boswell's Lessees v. Otis*, 9 How. 348 (1850); *Pomeroy's Equity Juris.*, § 1415. *Contra*, *Bird v. Calvert*, 22 S. C. 292 (1884).

² *Thornton v. Lane*, 11 Ga. 459 (1852); *Lane v. Harris*, 16 Id. 217 (1854); *McClaren v. Franciscus*, 43 Mo. 452 (1869); *New England, &c., Bank v. Newport Steam Factory*, 6 R. I. 154 (1859); *Priest*

v. Essex Manfg. Co., 115 Mass. 380 (1874); *Cambridge Water Works v. Somerville Dyeing, &c., Co.*, 4 Allen, 239 (1862); *Lindsley v. Simonds*, 2 Abb. Prac. (N. S.) 69 (1866); *Blake v. Hinkle*, 10 Yerg. 218 (1836); *Shellington v. Howland*, 53 N. Y. 371 (1873); *Wehrman v. Reakirt*, 1 Cin. Super. Ct. 230 (1871); *Dauchy v. Brown*, 24 Vt. 197; *Drinkwater v. Portland Marine Ry.*, 18 Me. 35 (1841); *Handy v. Draper*, 89 N. Y. 334 (1882). Cf. *Perkins v. Church*, 31 Barb. 84 (1859).

³ *Rocky Mountain National Bank v. Bliss*, 89 N. Y. 338 (1882). In this case it is held that a proceeding *in rem*, affecting only the property of the corporation attached, and execution against that property, is not what the rule requires; and again that the recovery of a judgment and issue of execution in another State is not a compliance with the rule, but that a judgment in and execution issued out of a court of the State where the statute is in force is necessary. To the same effect see *Brice v. Munro*, 5 Canadian Law Times, 130, Ontario High Court of Justice, Queen's Bench Division (1885), in which case it is held that an execution issued and returned in Quebec is not sufficient as against a company incorporated and existing in Ontario.

This rule is founded in reason and a wise public policy relative to the transaction of business, since the corporate funds are the corporate creditors' primary resource, even where the liability of the individual shareholder is declared to be primary like that of an original contractor or partner.¹ But where the corporation has been adjudged a bankrupt, and a dissolution has in this way been brought about, the remedy against the corporation need not first be exhausted.² Nor is it necessary in a case where the corporation is notoriously insolvent,³ or is formally dissolved.⁴ The record of the judgment against the corporation is competent evidence of the fact that the plaintiff is a corporate creditor, and of the amount due him.⁵

¹ *Stone v. Wiggin*, 5 Metc. 316 (1842); *Stedman v. Eveleth*, 6 Id. 114 (1843); *Leland v. Marsh*, 16 Mass. 389 (1820); *Marcy v. Clark*, 17 Id. 330 (1821).

² *State Savings Association v. Kellogg*, 52 Mo. 583 (1878); *Dryden v. Kellogg*, 2 Mo. App. 87 (1876); *Shellington v. Howland*, 53 N. Y. 371 (1873). *Cf.* *Ansonia Brass & Copper Co. v. New Lamp Chimney Co.*, 53 N. Y. 123 (1873); s. c. 91 U. S. 556; *Lovett v. Cornwell*, 6 Wend. 369 (1831); *People v. Bartlett*, 3 Hill, 570 (1842); *Loomis v. Tift*, 16 Barb. 541 (1853); *Walser v. Seligman*, 21 Blatchf. 130 (1881). And see *contra*, *Birmingham National Bank v. Mosser*, 14 Hun, 605 (1878).

³ *Hodges v. Silver Hill Mining Co.*, 9 Oregon, 200 (1881); *Terry v. Tubman*, 92 U. S. 156 (1875); *Camden v. Doremis*, 3 How. 533 (1845); *Reynolds v. Douglas*, 12 Peters, 497 (1836); *Kimber v. Bank of Fulton*, 49 Ga. 419. The right of action accrues to the creditor whenever it is clear that the corporation has no property from which the claim can be paid. A judgment is not necessary for the beginning of an action against the stockholder, though it may be necessary as evidence in such action to determine the measure of damages. *First Nat. Bank of Garretttsville v. Galene*, 64 Iowa, 445 (1884). *Cf.* *Cleveland v. Marine Bank*, 17 Wis. 545 (1863).

⁴ *Kincaid v. Dwinelle*, 59 N. Y. 548 (1875). *Cf.* *Hollingshead v. Woodward*, 35 Hun, 410 (1885). As to what is sufficient to dissolve a corporation for this purpose, see *Kincaid v. Dwinelle*, *supra*. Under a statute requiring dissolution of the corporation before corporate creditors can reach unpaid subscriptions,

the corporation is deemed to be dissolved when it has ceased to exercise its proper functions, is without funds and indebted. *Penniman v. Briggs*, 1 Hopk. Chan. (N. Y.) 343 (1824); *Slee v. Bloom*, 19 Johns. 456 (1822); *Bank of Poughkeepsie v. Ibbotson*, 24 Wend. 479 (1840). *Cf.* *Terry v. Anderson*, 95 U. S. 628 (1877). *Remington v. Samana Bay Co.*, 140 Mass. 494 (1886), holds that the judgment herein against the corporation is void if the corporation has been dissolved. It has been said that corporate creditors need not await the collection by the corporation of doubtful claims, but may compel the payment of their claims by the shareholders, and let them take the risk and delay. "Creditors," says the Supreme Court of Tennessee, "will not be required to await the collection of doubtful claims or claims in litigation. The stockholders must pay promptly, and take upon themselves the onus of delay and risk as to all such cases." *Moses v. Ocoee Bank*, 1 Lea, 398 414 (1878). See also *Stark v. Burke*, 9 La. Ann. 341. General creditors may also reach unpaid subscriptions, although another corporate creditor has a mortgage lien on the corporate property, rights, privileges, and franchises. *Dean v. Biggs*, 25 Hun, 122 (1881).

⁵ *Stephen v. Fox*, 83 N. Y. 313 (1881). The English rule upon this point is the same as the one prevailing in this country. There, accordingly, in those cases in which a judgment against a company can be enforced against a shareholder, a *scire facias* is a necessary preliminary, unless there is some statutory enactment to the contrary. 2 *Lindley on Partnership*, 520; *Partlett v. Pentland*, 1 Barn. & Ad. 704 (1831); *Clowes v. Brettell*, 10 Mee. & W.

§ 201. *The remedy by garnishment or attachment.*—There are various remedies which corporate creditors may employ to enforce the payment of partially paid up subscriptions. Among these is that of garnishment. Thus where a subscription has been called in, in part or wholly, and has not been paid by the subscriber, it is, at least to the extent of such calls, an asset of the corporation, and, like other assets, is subject to garnishment at the instance of a corporate creditor.¹

When, therefore, a stockholder is in default for installments of stock, for which calls have been made, he stands in the attitude of any other debtor to the corporation, and may be garnished in the usual way, upon the theory of the authorities just cited, for the purpose of collecting the corporation's debt. But this remedy is not available to reach that part of the unpaid subscription for which calls have not been made.²

506 (1842); *Winfield v. Barton*, 2 Dowl. (N. S.) 355 (1872); s. c. 7 Jur. 258; *Wingfield v. Peel*, 12 L. J. (N. S.) 102, Q. B. (1842).

¹ *Meints v. East St. Louis, &c., Co.*, 89 Ill. 48 (1878); *Hannah v. The Moberly Bank*, 67 Mo. 678 (1878); *Simpson v. Reynolds*, 71 Id. 594 (1880); *Faul v. Alaska, &c., Mining Co.*, 8 Sawyer, 420 (1882); *Curry v. Woodward*, 53 Ala. 371 (1875); *Bingham v. Rushing*, 5 Ala. 403; *Hays v. Lycoming, &c., Co.*, 99 Penn. St. 621 (1882). *Cf.* *Rand v. White Mountains R. R. Co.*, 40 N. H. 79 (1860); *Brown v. Union Insurance Co.*, 3 La. Ann. 177 (1848); *Angell and Ames on Corp.*, § 517; *Thomp. on Liab. of Stock*, §§ 265, 276, 317. See *Dean v. Biggs*, 25 Hun, 122 (1881).

² *Bingham v. Rushing*, 5 Ala. 403 (1843); *Brown v. Union Insurance Co.*, 3 La. Ann. 177 (1848); *Bunn's Appeal*, 105 Penn. St. 49 (1884). See also *Coalfield Coal Co. v. Peck*, 98 Ill. 139 (1881). In Nevada the right of garnishment in a case where calls had not been made, was expressly denied. *McKelvey v. Crockett*, 18 Nev. 238 (1884). *Cf.* *Meints v. East St. Louis, &c., Co.*, 89 Ill. 48 (1878); *Hughes v. Oregonian Ry. Co.*, 11 Oreg. 158; *Peterson v. Sinclair*, 83 Penn. St. 250 (1877); *Langford v. Ottumwa Water Power Co.*, 59 Ia. 283 (1882); *Chandler v. Siddle*, 10 N. B. R. 236; *Re Glen Iron Works*, 20 Fed. Rep. 674; s. c. 17 Fed. Rep. 324 (Penn.). In New York, there is no process of garnishment, but instead thereof, an attachment

is allowed. Under an attachment against a foreign corporation, not chartered by the United States, the sheriff may levy upon the sums remaining unpaid upon a subscription to the capital stock of the corporation, the subscriber being within the county and having property therein; "or upon one or more shares of stock therein held by such a person, or transferred by him for the purpose of avoiding payment thereof." New York Code of Civil Procedure, § 646. This provision of the New York Code seems to authorize seizure of the stock to collect a corporate debt, whether calls have been made or not. See *Bartlett v. Drew*, 57 N. Y. 587 (1874); *Griffith v. Mangam*, 73 Id. 611 (1878). It has also been held that a corporate creditor, by an execution against the corporation, may reach an unpaid subscription, though no call has been made. *In re Glen Iron Works*, 17 Fed. Rep. 324 (1883); s. c. 20 Id. 674 (1884); *Cucullu v. Union Insurance Co.*, 2 Rob. (La.) 571 (1842). *Cf.* *Bunn's Appeal*, 14 Week. Notes Cases, 193; and see *Hannah v. The Moberly Bank*, 67 Mo. 678 (1878). But this is a somewhat questionable rule, and the remedy proposed by it is probably very seldom invoked.

In Missouri it is held that "a proceeding by motion foreexecution against a stockholder of an insolvent corporation is in no sense the institution of an independent suit, but a mere supplementary proceeding in aid of the execution against the corporation." *Kohn v. Lucas*, 17 Mo. App.

§ 202. *The remedy by mandamus.*—It is doubtful whether corporate creditors can, in this country, have recourse to the writ of *mandamus* to compel the officers of the corporation to make a call for the purpose of raising money to meet corporate obligations.¹

In the English courts a *mandamus* is sometimes awarded in these cases.² But in this country the question of calls is not usually of much importance in such cases. The corporation is generally insolvent; a bill is generally filed in a court of equity to collect and distribute all the assets, and calls on the subscriptions are made by the court itself.³

§ 203. *The remedy by action at law.*—Another remedy is by an action at law. It has been held that unpaid subscriptions, after call, may be enforced by an action at law brought directly against the delinquent subscriber, and that in such an action each subscriber is liable, not for his proportionate share, but to the full extent of his unpaid subscription.⁴

§ 204. *The remedy by bill in equity.*—The remedy most usually adopted by corporate creditors, to obtain the payment of their claims against the corporation from the unpaid balances of subscriptions due the corporation by the subscribers to the capital stock, is by a bill in equity. This is in the nature of a creditor's bill, reaching the equitable assets of the principal debtor. It is

29 (1885); *Paxton v. Talmage*, 2 West. Rep. 105 (Mo. 1885). In the case *Ogilvie v. Knox Ins. Co.* 22 How. 380 (1859), the court said: "The creditors of the corporation are seeking satisfaction out of the assets of the company to which the defendants are debtors. If the debts attached are sufficient to pay their demands, the creditors need look no further. They are not bound to settle up all the affairs of this corporation, and the equity between its various stockholders or partners, corporators, or debtors."

¹ *Dalton, &c. R. R. Co. v. McDaniel*, 56 Ga. 191 (1876); *Hatch v. Dana*, 101 U. S. 205 (1879). *Cf. Cucultu v. Union Insurance Co.*, 2 Rob. (La.) 573 (1842); *Allen v. Montgomery, &c.*, R. R. Co., 11 Ala. 437 (1847).

² *Queen v. Victoria Park Co.*, 1 Ad. & El. (N. S.) 544; *Queen v. Ledyard*, Id. 616; *The King v. Katherine Dock Co.*, 4 Barn. & Ad. 360 (1832).

³ See Ch. VII.

⁴ *Bank of the United States v. Dallam*,

4 Dana, 574 (1836); *Allen v. Montgomery, &c.*, R. R. Co., 11 Ala. 437 (1847); *Faulk v. Alaska, &c.*, Mining Co., 8 Sawyer, 420 (1883); *Wilbur v. Stockholders*, 18 Bank. Reg. 178; *White v. Blum*, 4 Neb. 555 (1876); *McCarthy v. Lavasche*, 89 Ill. 270 (1878); *Bank of Poughkeepsie v. Ibbotson*, 24 Wend. 479 (1840). *Cf. Holmes v. Sherwood*, 3 McCrary, 405 (1881); s. c. 16 Fed. Rep. 725; *Corning v. Mohawk Valley Ins. Co.*, 11 How. Prac. 191 (1855). And see *Van Buren v. Chenango Ins. Co.*, 12 Barb. 675 (1852). The Supreme Court of the United States, however, has denied the existence of this remedy in favor of a creditor of a corporation organized under the general laws of Oregon. *Patterson v. Lynde*, 106 U. S. 519 (1882), saying that "No one creditor can assume that he alone is entitled to what any stockholder owes, and sue at law, so as to appropriate it exclusively to himself." *Cf. Terry v. Little*, 101 U. S. 216 (1879).

the most effectual, simple, and just remedy, and is not only the favorite remedy of the courts, but is generally resorted to by the corporate creditors themselves.¹ Some of the courts have even gone to the extent of holding a bill in equity to be the exclusive remedy for the corporate creditor in these cases.² Occasionally, also, statutes are enacted prescribing that a creditor who seeks to apply such assets to the payment of his claim can do so only by a suit in equity.³ The right to proceed by a suit in equity herein has been held to exist, although the general equitable remedy by creditors' bill has been abolished by statute.⁴

§ 205. *Parties to the bill in equity.*—(a.) *Parties plaintiff.*—
A corporate creditor who seeks in this way to obtain payment of

¹ *Pfohl v. Simpson*, 74 N. Y. 137 (1878); *Griffith v. Mangam*, 73 Id. 611 (1878); *Mathez v. Neidig*, 72 Id. 100 (1878); *Dayton v. Borst*, 31 Id. 435 (1865); *Mann v. Pentz*, 3 Id. 415 (1850); *Stephens v. Fox*, 83 Id. 313 (1881); s. c. 17 Hun, 435; *Ward v. Griswoldville Manfg. Co.*, 16 Conn. 593 (1844); *Bank of the United States v. Dallam*, 4 Dana, 574 (1836); *Crawford v. Rohrer*, 59 Md. 599 (1882); *Hightower v. Thornton*, 8 Ga. 486 (1850); *Hightower v. Mustian*, 8 Id. 506 (1850); *Dalton, &c., R. R. Co. v. McDaniel*, 56 Id. 191 (1876); *German-town, &c., Ry. Co. v. Fidler*, 60 Penn. St. 124 (1889); *Adler v. Milwaukee, &c., Co.*, 13 Wis. 57 (1860); *Curry v. Woodward*, 53 Ala. 371 (1875); *Allen v. Montgomery, &c., R. R. Co.*, 11 Id. 437 (1847); *Wincock v. Turpin*, 96 Ill. 135 (1880); *Henry v. Vermillion, &c., Turn-pike Co.*, 17 Ohio, 187 (1848); *Miers v. Zanesville and Maysville Turnpike Co.*, 11 Id. 273 (1842); *Judson v. Rossie*, 9 Pa. 381 (1842); *Van Pelt v. U. S. &c., Co.*, 13 Abb. Prac. (N. S.) 331 (1872). (Compare with this case *Sherwood v. Buffalo, &c., R. R. Co.*, 12 How. Prac. 137 (1855); *Hammond v. Hudson River, &c., Co.*, 11 Id. 33 (1854).) *Marsh v. Burroughs*, 1 Woods, 463 (1871); *Louisiana Paper Co. v. Waples*, 3 Id. 34 (1877); *Faul v. Alaska Mining, &c., Co.*, 8 Sawyer, 420 (1883); *Holmes v. Sher-wood*, 3 McCrary, 405 (1881); s. c. 16 Fed. Rep. 725; *Chandler v. Siddle*, 10 Bank. Reg. 236; *Myers v. Seeley*, 10 Id. 411; *Wilbur v. Stockholders*, 18 Id. 178; *Harmon v. Page*, 62 Cal. 448 (1882); *Ogilvie v. Knox Insurance Co.*, 22 How. 380 (1859); *Sanger v. Upton*, 91 U. S. 56,

60 (1875); *Hatch v. Dana*, 101 Id. 205 (1879); *Salman v. Hamborough Co.*, 1 Cas. in Chan. (Eng.) 204.

² *Jones v. Jarman*, 34 Ark. 323 (1879); *Harris v. First Parish in Dorchester*, 23 Pick. 112 (1839); *Knowlton v. Ackley*, 8 Cush. 93 (1861); *Erickson v. Nesmith*, 15 Gray, 221 (1860); *Smith v. Huckabee*, 53 Ala. 191 (1875); *Umsted v. Buskirk*, 17 Ohio, St. 113; *Pollard v. Bailey*, 20 Wall. 520 (1874); *Terry v. Little*, 101 U. S. 216 (1879). *Cf. Spear v. Grant*, 16 Mass. 9 (1819); *Hodges v. Silver Hill Mining Co.*, 9 Oregon, 200 (1881).

³ *Hadley v. Russell*, 40 N. Y. 109 (1860).

⁴ *Alder v. Milwaukee, &c., Manfg. Co.*, 13 Wis. 57 (1860). The equitable jurisdiction herein seems to have been based on various grounds. *Wilbur v. The Stockholders*, 18 Bank. Reg. 178. Thus, for example, the bill in equity in these cases has been held to be in the nature of an equitable attachment in which the subscribers are in effect, called on to answer as garnishees of the principal debtor. *Ogilvie v. Knox Insurance Co.*, 22 How. 380 (1859). In practice a receiver is usually appointed, the amount of the corporate debts and of the amount necessary to be contributed by the holders of shares not paid up is ascertained by proof, or through a referee and master's report, and then there is a final decree affording, as far as the assets admit, adequate relief, and, in any event, proportional relief to all parties. *Dalton, &c., R. R. Co. v. McDaniel*, 56 Ga. 191 (1876); *Wilbur v. The Stockholders*, 18 Bank. Reg. 178; *Ogilvie v. Knox Insurance Co.*, 22 How. 380 (1859).

his claim from the unpaid subscriptions to the capital stock of the corporation, should file his bill on behalf of himself and such other creditors as may wish to come in.¹ The general rule is that such a suit is and should be for the benefit of any or all creditors who elect to come in as parties complainant, and establish their debts according to the course and practice of a court of chancery.² While the bill must be so framed as to permit other creditors, if they elect, to come in and be made parties to the suit, it is, in no way, necessary to join them as parties. The other creditors are proper, but not necessary parties.³ Several creditors, however, cannot bring separate suits of this nature. They must all join in one proceeding.⁴ The stockholders need not wait to be made parties defendant to a creditors'

¹ *Crease v. Babcock*, 10 Metc. 525 (1846); *Holmes v. Sherwood*, 3 McCrary, 405 (1881); *Sawyer v. Hoag*, 17 Wall. 610 (1878); *Mills v. Scott*, 99 U.S. 25 (1878); *Patterson v. Lynde*, 106 Id. 519 (1882).

² *Wetherbee v. Baker*, 35 N. J. Eq. 501 (1882); *Coleman v. White*, 14 Wis. 700 (1862); *Carpenter v. Marine Bank*, 14 Id. 705, n. (1862); *Morgan v. New York, &c., R. R. Co.*, 10 Paige, 290 (1843); *Masters v. Rossie Lead Mining Co.*, 2 Sandf. Chan. 301 (1845); *Mann v. Pentz*, 3 N. Y. 415 (1850); *Umsted v. Buskirk*, 17 Ohio St. 113 (1866); *Crease v. Babcock*, 10 Metc. 525 (1846); *Pollard v. Bailey*, 20 Wall. 520 (1874); *Terry v. Little*, 101 U.S. 216 (1879). Any creditor has a right to come in, establish his claim and share *pro rata* in the distribution of the assets, even though the bill was not filed for the benefit of such as should choose to come in and share the expense. *Turnbull v. Prentiss Lumber Co.*, 55 Mich. 387 (1884). See also *Tallmadge v. Fishkill Iron Co.*, 4 Barb. 393 (1848); *Walker v. Crain*, 17 Id. 131 (1853). In consequence thereof no one creditor can, by superior diligence in filing a bill, obtain a preference over other creditors, in respect of the unpaid balances of subscriptions. *Vide* the cases in last note. There is, however, an earlier case in the Ohio reports, which seems to recognize such a preference. *Miers v. Zanesville and Maysville Turnpike Co.*, 13 Ohio, 197 (1844). See *Adler v. Milwaukee, &c., Co.*, 13 Wis. 57 (1868); *Wright v. McCormack*, 17 Ohio St. 86 (1866).

³ *Marsh v. Burroughs*, 1 Woods, 463 (1871); *Crease v. Babcock*, 10 Metc. 525

(1846); *Hatch v. Dana*, 101 U. S. 205 (1879). *Cf. Adler v. Milwaukee, &c., Co.*, 13 Wis. 57 (1860).

⁴ *Crease v. Babcock*, 10 Metc. 525 (1846). But see *Perry v. Turner*, 55 Mo. 418 (1874). And an action to compel the payment of an unpaid subscription may be joined by a creditor with an action to enforce a statutory liability. *Warner v. Callender*, 20 Ohio St. 190 (1870). Accordingly, where a bill is filed, on behalf of all the creditors who chose to come in, against all the stockholders in default, the courts will enjoin a separate creditor's suit. *Pierce v. Milwaukee Construction Co.*, 38 Wis. 253 (1875). *Cf. Coleman v. White*, 14 Id. 700 (1862); *Carpenter v. Marine Bank*, 14 Id. 705, n. (1862); *Ballston Spa Bank v. Marine Bank*, 18 Id. 490 (1864). A stockholder himself, although he is in default, provided he is solvent, may, if he is also a creditor of the corporation, be a party to the bill to collect the unpaid subscriptions, but pursuant to the final decree he must contribute ratably with the rest. *Bissit v. Kentucky River Navigation Co.*, 15 Fed. Rep. 353, and the valuable note; *Thompson v. Reno Savings Bank*, 10 Am. & Eng. Corp. Cas. 202 (Nev., 1885). *Cf. Hogg's Appeal*, 88 Penn. St. 195 (1878); *Calhoun v. The Steam Ferry Boat, &c.*, 27 Int. Rev. Rec. 273 (1881), in which case it is held he cannot sue the corporation. But see *Milvain v. Mather*, 5 Exch. 55 (1850), in which it is held that a corporation sued by a stockholder may set off any amount due by him on calls. *Cf. Ex parte Winsor*, 3 Story's C. C. 411 (1844).

bill before moving for contribution, but may, in a proper case, before a suit in the nature of a creditors' bill is filed against them by creditors of the corporation, file a bill in equity upon their own account, making the corporation a party, to enforce the payment of unpaid balances of subscription, for the payment of corporate indebtedness, and for contribution.¹

§ 206. (b.) *Parties defendant.*—The defendants to such a suit should be the corporation itself,² and all from whom an unpaid subscription is due, except such as are unknown or insolvent, or beyond the jurisdiction.³

¹ *Fiery v. Emmert*, 36 Md. 464 (1872).

² The corporation is ordinarily a necessary party. *Mann v. Pentz*, 3 N. Y. 415 (1850); *Walsh v. Memphis, &c., R. R. Co.*, 2 McCrary, 156 (1881); s. o. 19 Fed. Rep. 152; *Wilbur v. The Stockholders*, 18 Bank. Reg. 178; *Wetherbee v. Baker*, 35 N. J. Eq. 501 (1882). But see *contra*, *Walser v. Seligman*, 21 Blatchf. 130 (1882), a well considered case, and *Wellman v. Howland Coal & Iron Works*, 19 Fed. Rep. 51. In the case last cited it was held that where a corporation is without property or officers, or place of business, it need not be made a party of record.

³ *Vick v. Lane*, 56 Miss. 681 (1879); *Walsh v. Memphis, &c., R. R. Co.*, 2 McCrary, 156 (1881); *Hadley v. Russell*, 40 N. H. 109 (1860); *Erickson v. Nesmith*, 46 Id. 371 (1860); *Pierce v. Milwaukee, &c., Co.*, 38 Wis. 253 (1875); *Coleman v. White*, 14 Id. 700 (1862); *Carpenter v. Marine Bank*, 14 Id. 705, n. (1862); *Umsted v. Buskirk*, 17 Ohio St. 113 (1866); *Mann v. Pentz*, 3 N. Y. 415 (1850). Cf. *Young v. New York & Liverpool Steamship Co.*, 10 Abb. Prac. 299 (1860). The bill should contain an appropriate allegation as to the shareholders unknown, insolvent, or out of the jurisdiction, and a prayer that, upon discovery, they be made parties when possible. *Bogardus v. Rosendale Manufacturing Co.*, 17 N. Y. 147 (1852). "Where the attempt is to reach the liability of the shareholders on their subscription to capital stock, all the solvent stockholders within the jurisdiction must be joined, except where this will be excused upon an allegation that the number is too great." *Chalmers, J.*, in *Vick v. Lane*, 56 Miss. 681, 684 (1879). Cf. *Bonewitz v. Van Wert Co. Bank*, 41 Ohio St. 78 (1884). But on the other hand, with respect to the matter of join-

ing all the solvent shareholders who are in arrears as parties defendant to the bill, provided they are within the jurisdiction, we find a line of authorities in support of the proposition that all such stockholders are not always necessary parties to the bill, that such a suit may properly be brought against one, or any, of the delinquent stockholders as well as against all, and that a bill will not be held defective merely because it fails to include all the delinquent stockholders as parties defendant. *Ogilvie v. Knox Insurance Co.*, 22 How. 380 (1859); *Hatch v. Dana*, 101 U. S. 205 (1879); *Marsh v. Burroughs*, 1 Woods, 463 (1871); *Holmes v. Sherwood*, 3 McCrary, 405 (1881); *Glenn v. Williams*, 60 Md. 93 (1882); *Bartlett v. Drew*, 57 N. Y. 587 (1874); *Griffith v. Mangam*, 73 Id. 611 (1878); *Brundage v. Monumental, &c., Mining Co.*, 12 Oregon, 322 (1885). Cf. *Von Schmidt v. Huntington*, 1 Cal. 55 (1850); *Lamar Insurance Co. v. Gulick*, 102 Ill. 41 (1882). Perhaps a distinction may properly be made with reference to the joinder of parties defendant between the case of a bill filed for the purpose of effecting a winding up of an insolvent company, and the reaching of all the corporate assets on the one hand, and a bill, on the other hand, which looks only to the collection of a debt out of unpaid stock subscriptions. It seems that a corporate creditor may sometimes properly elect to pursue his remedy against one or any of the delinquent shareholders without undertaking to adjust and determine all the intervening equities between the shareholders and creditors. That is to say, that he may collect his debt out of the unpaid balance due the corporation by any one or more shareholders, leaving the shareholders who pay him to look to the other delinquent subscribers for contribution, if there is a case for contribu-

The stockholders against whom the bill is filed may, however, it seems, when all are not made parties, file a cross bill, obtain a discovery of the remaining delinquent stockholders, bring them in as parties, and thus enforce contribution.¹ And, upon plain principles of equity jurisprudence, if all the parties who are liable have not been brought before the court, those who are defendants of record cannot be charged with liability which should fall upon those who are absent, unless it be shown that the absentees are insolvent, or beyond the jurisdiction of the court.²

tion, the complainant becoming himself liable to other corporate creditors in case he receive more than his proportion of corporate assets. In such a case it is not necessary to join all the stockholders. The bill may properly be filed against one or any of them. But if the winding up of the company is involved, the bill ought to make them all parties defendant. *Brundage v. Monumental, &c., Mining Co.*, 12 Oregon, 322 (1885); *Bartlett v. Drew*, 57 N. Y. 587 (1874); *Hatch v. Dana*, 101 U. S. 205 (1879). In *Hatch v. Dana*, *supra*, there was a bill to compel payment of a debt out of the unpaid subscription of a single stockholder. It was not sought to wind up the company. It being urged that a creditor of an insolvent corporation is not at liberty to proceed against one or more delinquent subscribers to recover the amount of his debt, without an account being taken of other indebtedness, and without bringing in all the stockholders for contribution, the court, by Mr. Justice Strong, said: "The liability of a subscriber for the capital stock of a company is several and not joint. By his subscription each becomes a several debtor to the company, as much so as if he had given his promissory note for the amount of his subscription. At law, certainly his subscription may be enforced against him without joinder of other subscribers, and in equity his liability does not cease to be several. A creditor's bill merely subrogates the creditor to the place of the debtor, and garnishes the debt due to the indebted corporation. It does not change the character of the debt attached or garnished. It may be that if the object of the bill is to wind up the affairs of this company, all the shareholders, at least so far as they can be ascertained, should be made parties, that complete justice may be done by equaliz-

ing the burdens, and in order to prevent a multiplicity of suits. But this is no such case. The most that can be said, is that the presence of all the stockholders might be convenient, not that it is necessary. When the only object of a bill is to obtain payment of a judgment against a corporation, out of its credits or intangible property, that is, out of its unpaid stock, there is not the same reason for requiring all the stockholders to be made defendants." See also *Bonewitz v. Van Wert Co. Bank*, 41 Ohio St. 78; *Bartlett v. Drew*, 57 N. Y. 587, 589, 591 (1874). As to when bills brought by creditors in these cases are and are not multifarious, see *Allen v. Montgomery, R. R. Co.*, 11 Ala. 437 (1847); *Brinkerhoff v. Brown*, 7 Johns. Chan. 217 (1823); *Cambridge, &c., Co. v. Somerville, &c., Co.*, 4 Allen, 239 (1862); *Barre National Bank v. Hingham Mfg. Co.*, 127 Mass. 563 (1879); *Pope v. Leonard*, 115 Id. 286 (1874); *Deaderick v. Wilson*, 8 Baxter, 108 (1874).

¹ *Hatch v. Dana*, 101 U. S. 205 (1879). In the original bill itself there may properly be a prayer, when some of the delinquent shareholders are unknown, for a discovery, in order that such unknown stockholders may be made parties by amendment. *Bogardus v. Rosendale Mfg. Co.*, 7 N. Y. 147 (1852).

² *Wood v. Dummer*, 3 Mason, 307 (1824); *Marsh v. Burroughs*, 1 Woods, 463 (1871); *Bonewitz v. Van Wert Co. Bank*, 41 Ohio St. 78 (1884). *Cf. Erickson v. Nesmith*, 46 N. H. 371 (1860). When there are delinquent stockholders beyond the jurisdiction, the stockholders who have been sued and compelled to pay more than their due proportion, must look to them for contribution by an appropriate proceeding. *Holmes v. Sherwood*, 3 McCrary, 405 (1881).

§ 207. *A court of equity may make a call.*—It is well settled,¹ that, when stock is subscribed to be paid in upon call by the corporate authorities, and the company neglects or refuses to make such calls as are necessary to raise funds to meet the just corporate obligations, a court of equity will itself make the necessary calls, if the interests of the creditors require it; that is to say, the court will, in behalf of the creditors, do what it is the duty of the corporation to do in respect of calls.² And the court may make the call although the statute says calls shall be made by the trustees.³

§ 208. *Receivers and assignees in bankruptcy for the benefit of creditors.—Their duties, powers, and liabilities as to unpaid subscriptions.*—When a corporation becomes insolvent, with corporate creditors on the one hand pressing their claims, and subscriptions to the capital stock wholly or partially uncollected on the other hand, it is usual to place the assets of the company, including the claims against delinquent shareowners, in the hands of an indifferent third person for the benefit of all concerned. Such a person may be an assignee under State insolvent laws, a receiver of an assignee in bankruptcy. A receiver in such a case may be defined to be a third person appointed by a court of equity, to act as the representative alike of creditors and stockholders for the purpose of collecting the corporate assets and paying the corporate debts.⁴ It is the right and duty of such a

¹ *Vide* Chap. VII, § 108, *supra*.

² *Scovill v. Thayer*, 105 U. S. 143, 155 (1881); *Hatch v. Dana*, 101 Id. 205, 214 (1879); *Curry v. Woodward*, 53 Ala. 371 (1875); *Wilbur v. Stockholders*, 18 Bank. Reg. 178; *Marsh v. Burroughs*, 1 Woods, 463 (1871); *Myers v. Seeley*, 10 Bank. Reg. 411; *Henry v. Vermillion, &c.*, R. R. Co., 17 Ohio, 187 (1848); *Robinson v. Bank of Darien*, 18 Ga. 65; *Ward v. Griswoldsville Mfg. Co.*, 16 Conn. 593 (1844); *Sanger v. Upton*, 91 U. S. 56, (1875); *Chubb v. Upton*, 95 Id. 665 (1877); *Glenn v. Semple*, Ala. (1885); *Glenn v. Williams*, 60 Md. 93. *Cf.* *Germanatown, &c. Ry. Co. v. Fitler*, 60 Penn. St. 124 (1869); *Chandler v. Keith*, 42 Iowa, 99 (1875); *Mann v. Pentz*, 3 N. Y. 415 (1850); *Ogilvie v. Knox Insurance Co.*, 22 How. 380 (1871); *Adler v. Milwaukee Mfg. Co.*, 13 Wis. 62 (1860);

and see *Seymour v. Sturgess*, 26 N. Y. 134 (1862); *Wheeler v. Millar*, 90 Id. 353 (1882.)

³ *Crawford v. Rohrer*, 59 Md. 599 (1882). *Cf.* *Glenn v. Saxton*, California (1886). Where it was provided by the charter of the corporation that all calls are to be made only upon a three-fourths vote of the stockholders, it was held that a call by the court was irregular. *Trustees of the Louisiana Paper Co. v. Waples*, 3 Woods, 34 (1877). *Cf.* *Burlington, &c., R. R. Co. v. Boestler*, 15 Iowa, 555 (1864); *Penobscot, &c., R. R. Co. v. Dunn*, 39 Me. 587 (1855); *Philadelphia, &c., R. R. Co. v. Hickman*, 28 Penn. St. 318 (1857); *Carlisle v. Cahawba, &c., R. R. Co.*, 4 Ala. 70 (1842).

⁴ *Johnson v. Laffin*, 5 Dill. 65 (1878); *High on Receivers* (2d edition), 1.

receiver to collect the unpaid subscriptions, so far as it may be necessary, for the purpose of paying the corporate debts in full.¹

As incidental to the receiver's power to collect unpaid balances of subscription, it is held that he may, as an officer of the court, make calls for the amount due.²

As against the delinquent subscribers the receiver stands in the position of the corporation. He has all the rights as regards the collection of the assets, including the claims against the stockholders, which the corporation possessed before its insolvency, and, in this respect, his powers are neither more nor less than those of the corporate officers under ordinary circumstances.³ Accordingly the receiver of a foreign corporation, duly empowered to sue at home, may sue resident stockholders for the balances due the company, provided the corporation itself could have done so had the stockholder been a resident of the State of its domicile.⁴

¹ *Dayton v. Borst*, 31 N. Y. 435 (1865); *Nathan v. Whitlock*, 9 Paige, 152 (1841); *Frank v. Morrison*, 58 Md. 423 (1882); *Chandler v. Brown*, 77 Ill. 333 (1875). This right of the receiver was denied, in some early cases, but it is now probably everywhere conceded. See *Hadley v. Russell*, 40 N. H. 109 (1860); *Coleman v. White*, 14 Wis. 700 (1862); *Umsted v. Buskirk*, 17 Ohio St. 113 (1866). The receiver's action to collect should, it is held in Mississippi, be at law. *Freeman v. Winchester*, 18 Miss. 577 (1848). While in New York, under the older practice, it was held that it must be in equity. *Sagory v. Dubois*, 3 Sandf. Chan. 466. At present, by statute, this action in New York may be either at law or in equity. 3 R. S. Chap. VIII, Art. 3, § 69. Cf. *Harmon v. Page*, 62 Cal. 448 (1882.)

² *Dane v. Young*, 61 Me. 160 (1872); *Hall v. United States Insurance Co.*, 5 Gill (Md.), 484 (1847); *Hightower v. Thornton*, 8 Ga. 486 (1850); *Rankine v. Elliott*, 16 N. Y. 377 (1857). But see *In re Birmingham, &c. Ry. Co.*, L. R., 18 Char. Div. 155 (1881), when a railway receiver is held, it seems, not to have such a power. This is a case, however, under the English Railway Companies Act, 1867. See also *Nathan v. Whitlock*, 9 Paige, 152 (1841); *Chandler v. Keith*, 42 Iowa, 99 (1875). In *Mann v. Pentz*,

3 N. Y. 415 (1850), it is insisted that the proper way to collect unpaid subscriptions is by a creditor's bill against the corporation and the delinquent shareholders, to be filed by a creditor, even when the property is in the hands of a receiver. It is doubtful, however, whether this practice would now be followed. A receiver is sometimes given expressly the same power to make calls that the corporate officers had before the sequestration. *Hall v. United States Insurance Co.*, *supra*.

³ *Cutting v. Damerel*, 88 N. Y. 410 (1882); *Mean's Appeal*, 85 Penn. St. 293 (1877); *Angell and Ames on Corp.* § 520. It may be remarked here, that the receiver has no power to enforce statutory liability, this liability not being an asset of the corporation. See *Farnsworth v. Wood*, 91 N. Y. 308 (1883), and the Chapter on Statutory Liability, *infra*.

⁴ *Dayton v. Borst*, 31 N. Y. 435 (1865), a case where a receiver appointed by the Court of Chancery in New Jersey, was held competent to maintain a suit of this nature in New York against a citizen thereof. Cf. *Tinkham v. Borst*, 31 Barb. 407 (1860); *McDonough v. Phelps*, 15 How. Prac., 372 (1856); *Seymour v. Sturgess*, 26 N. Y., 134 (1862). It has been held that a receiver may collect unpaid balances due on subscriptions, although the other corporate assets have

The receiver, moreover, has no greater or higher right than the corporation to collect unpaid subscriptions, and where the corporation could not have maintained an action upon such a subscription, the receiver cannot.¹

As long as the authority of the receiver subsists, a creditor cannot directly bring suit against delinquent shareowners, but the receiver may be compelled to act in the matter at the instance of creditors.²

As assignee for the benefit of the creditors of a corporation, like a receiver, represents both the corporation and the creditors, and should collect unpaid subscriptions;³ and, in like manner, an assignee in bankruptcy may sue to recover the amounts due by stockholders on account of their subscriptions, and his proper remedy is by bill in equity, making all the delinquent shareowners parties to the bill.⁴

not been collected and the amount of the liabilities is undetermined. *Starke v. Burke*, 9 La. Ann. 341 (1854), and that if, on the final settlement, there is a surplus, it is to be returned *pro rata* to the shareholders. *Pentz v. Hawley*, 1 Barb. Chan. (N. Y.) 122 (1846). But the more modern and better rule is that a receiver has no authority to call upon a subscriber for his unpaid balance until the court have determined the amount of the corporate indebtedness and fixed definitely the liability of each share of the stock. *Chandler v. Keith*, 42 Iowa, 99 (1875). See also *Mills v. Scott*, 99 U. S., 25 (1878); *Cleveland v. Burnham*, 55 Wis. 598 (1885).

¹ *Billings v. Robinson*, 94 N. Y. 415 (1884); affirming 28 Hun, 122. The court cannot give a receiver power to compromise claims upon unpaid subscriptions. *Chandler v. Brown*, 77 Ill. 333 (1875). See § 210.

² It is the receiver's duty, as we have seen, to act promptly and vigilantly in the collection of the assets, and to compel payment of balances due by subscribers on unpaid stock, if such a course is necessary to meet the demands of creditors. If the receiver fails to do his duty in this respect, the creditors may compel him to act, inasmuch as they cannot act directly themselves. *Gas Light Co. v. Haynes*, 7 La. Ann. 114 (1852); *New Orleans Gas Light Co. v.*

Bennett, 6 Id. 457 (1851); *Starke v. Burke*, 9 Id. 341 (1854). *Cf.* *Atwood v. Rhode Island Agricultural Bank*, 1 R. I. 376 (1850); *Eppricht v. Nickerson*, 78 Mo. 482 (1884). *Contra*, *Mann v. Pentz*, 3 N. Y. 415 (1850). This case, as has been intimated in a former note (*q. v.*), is not, upon this point, considered good law. When the receiver stated in his answer that he did not deem it his duty to sue the stockholders on behalf of the creditors, it was held that the creditors themselves were authorized to commence suit in their own behalf, against the stockholders, without first requesting the receiver to sue them. *Atwood v. Rhode Island Agric. Bank*, *supra*.

³ *Shockley v. Fisher*, 75 Mo. 498 (1882). *Cf.* *Germantown, &c., Ry. Co. v. Fitler*, 60 Penn. St. 124 (1869).

⁴ *Sawyer v. Hoag*, 17 Wall. 610, 621 (1873); *Upton v. Tribilcock*, 91 U. S. 45 (1875); *Sanger v. Upton*, Id. 56; *Webster v. Upton*, Id. 65; *Chubb v. Upton*, 95 Id. 665 (1877); *Payson v. Stoeve*, 2 Dill. 427 (1873); *Upton v. Hansbrough*, 3 Biss. 417 (1873). *Cf.* *County of Morgan v. Allen*, 103 U. S. 498 (1880). The principles of equity applicable in cases of this nature to actions by a receiver will, in general, unless some statute has changed the law, be found applicable to these actions when brought by assignees at common law or in bankruptcy.

§ 209. *The judgment against the corporation impeachable only for fraud, or want of jurisdiction.*—That a judgment conclusively settles all matters of controversy involved in the suit, so far as parties or their privies are concerned, excepting where it may be impeached for fraud or want of jurisdiction, is well established law. When, therefore, a corporate creditor has obtained judgment against the corporation, and execution is returned unsatisfied, and he then proceeds to enforce his remedy against the holders of stock not paid up, the question arises whether the stockholder may set up in defense matters which the corporation might have set up or did set up.

It has been strenuously insisted that he might. This was Chancellor Kent's famous contention in the case of *Slee v. Bloom*,¹ but the authorities have firmly established the rule that, in the absence of fraud and collusion, judgments against the corporation, if the court had jurisdiction, are conclusive against the stockholders as to the validity and amount of the creditor's claim.² Thus it is held that the stockholder cannot take advantage, in the suit against him, of a defect in the service of process upon the corporation in the original suit. His remedy in such a case is by a direct proceeding.³ There is, however, a line of

¹ 5 Johns. Chan. 366 (1820); reversed by 19 Johns. 456; s. c. Id. 669, by Spencer, C. J.

² *Slee v. Bloom*, 20 Johns. 669 (1822); *Henry v. Vermillion, &c., R. R. Co.*, 17 Ohio, 187 (1848); *Hampson v. Weare*, 4 Iowa, 13 (1856); *Milliken v. Whitehouse*, 49 Me. 527 (1860); *Merrill v. Suffolk Bank*, 31 Id. 57 (1849); *Wilson v. Pittsburgh, &c., Coal Co.*, 43 Penn. St. 424 (1862); *Bank of Wooster v. Stevens*, 1 Ohio St. 233 (1853); *Conway v. Duncan*, 28 Id. 102 (1875); *Stephens v. Fox*, 83 N. Y. 313 (1881); *Chaffin v. City of St. Louis*, 4 Dill. 24 (1876); *Marsh v. Burroughs*, 1 Woods, 463 (1871); *Glenn v. Springs*, 26 Fed. Rep. 494 (1885); *Grund v. Tucker*, 5 Kan. 70 (1869); *Graham v. Boston, Hartford & Erie R. R. Co.*, 118 U. S. 161 (1886); *Bissitt v. Kentucky River Navigation Co.*, 15 Fed. Rep. 353 (1882); *Hawes v. Petroleum Co.*, 101 Mass. 385; *Morawetz on Corp.*, § 619; *Bank of Australasia v. Nias*, 16 Q. B. 717 (1851); s. c. 20 L. J. (N. S.) Q. B. 284. So also in actions to enforce statutory liability of stockholders, a judgment against

the corporation is equally conclusive. *Donworth v. Coolbaugh*, 5 Iowa, 300 (1857); *Came v. Brigham*, 39 Me. 35 (1854); *Gaskill v. Dudley*, 6 Metc. 546 (1843); *Hawes v. Anglo-Saxon Petroleum Co.*, 101 Mass. 385 (1869); *Johnson v. Somerville, &c., Co.*, 15 Gray, 216 (1860); *Boyd v. Hall*, 56 Ga. 563 (1876); *Stephens v. Fox*, 83 N. Y. 313 (1881); *Holyoke Bank v. Goodman Paper Manfg. Co.*, 9 Cush. 576 (1852); 1 Herman on Estoppel and Res Judicata, 165; *Thomp. Liabil. of Stockh.*, § 329; *Bigelow on Estoppel*, 89; *Freeman on Judgments*, § 178. The stockholder may, of course, set up that he is not a stockholder, and other similar defenses, such as are specified in Chap. X. See *infra*, § 210.

³ *Came v. Brigham*, 39 Me. 35 (1854); *Wheeler v. Millar*, 24 Hun, 541 (1881). See also *Louisville, &c., R. R. Co. v. Letson*, 2 How. 497 (1844). Nor can he set up that the creditors' rights are based on purchases made *ultra vires* by the corporate officers. *Sumner v. Marcy*, 3 Woodb. & M. 105 (1847). In this case it was said that the stockholder's remedy was by bill

cases holding that judgment against the corporation is only *prima facie* evidence against the shareholder in an action to subject the balance due on his subscription to the payment of the debt.¹ But this is an exceptional doctrine.² In New York the conclusiveness of the judgment in these cases has been much questioned.³

§ 210. *Defenses in actions to compel payment of balances of subscriptions, available against corporate creditors.*—There are, of course, certain defenses which subscribers may set up when actions are brought against them on behalf of corporate creditors. But both in England and in this country the courts do not favor such defenses, especially after the corporation has become insolvent. There are many defenses which might defeat the corporation in its action, which would not prevent the corporate creditor from enforcing the subscription.⁴

in equity to enjoin further proceedings in the suit at law.

In *Chestnut v. Pennell*, 92 Ill. 55 (1879), it was held that a decree against the corporation is not admissible in evidence against a stockholder who was not a party to the bill or decree, actually or constructively, and that in such a case proof of the liability of the corporation to the creditor should be given. *Cf.* *Washington Bank v. Palmer*, 2 Sandf. Super. Ct. 686 (1850); *New York, &c., R. R. Co. v. Cook*, Id. 732 (1850). Clerical errors on the part of officers of the court who levy assessments, are errors which may be corrected in the suit against the shareowner, and so of certain errors of judgment. *Hurd v. Tallman*, 60 Barb. 272 (1871); *Payson v. Stoeve*, 2 Dill. 427 (1873); *Upton v. Hansbrough*, 2 Biss. 417 (1873); *Sanger v. Upton*, 91 U. S. 56, 62 (1875).

¹ *Grund v. Tucker*, 5 Kan. 70 (1869); *Stephens v. Fox*, 83 N. Y. 313 (1881); *Merchants' Bank v. Chandler*, 19 Wis. 435 (1865); *Berger v. Williams*, 4 McLean, 577 (1849); *Belmont v. Coleman*, 1 Bosw. 188 (1857). *Cf.* s. c. 21 N. Y. 96 (1860). See also *Bigelow on Estoppel*, 89; *Thomp. on Liability of Stockh.*, § 329, note. And *cf.* *McMahon v. Macy*, 51 N. Y. 155, 165 (1872).

² Where the stockholders are liable only on a particular class of corporate debts, or to certain classes of creditors only, the court will not, of course, reject evidence tending to show either that the debt recovered belongs or does not belong

to the class on which the shareholder sued is liable. *Wilson v. The Stockholders*, 43 Penn. St. 424 (1862); *Conant v. Van Schaick*, 24 Barb. 87 (1857); *Larabee v. Baldwin*, 35 Cal. 135 (1868). *Cf.* *Hudson v. Carman*, 41 Me. 84 (1856).

³ *Slee v. Bloom*, 5 Johns. Chan. 366 (1820); reversed, *Slee v. Bloom*, 20 Johns. 669 (1822). But the mischief was not thereby wholly undone, and we find in the New York reports a long line of subsequent cases in which various grounds upon this subject are taken. See *Mcoss v. Oakley*, 2 Hill, 265 (1842); *Moss v. McCullough*, 5 Id. 181 (1843). See a final determination of this case in 7 Barb. 279 (1849); *Belmont v. Coleman*, 1 Bosw. 188 (1857); s. c. 21 N. Y. 96 (1860); *Strong v. Wheaton*, 38 Barb. 616 (1861); *Conklin v. Furman*, 8 Abb. Prac. (N. S.) 161 (1865); *Moss v. Aversell*, 10 N. Y. 450 (1853); *Miller v. White*, 50 N. Y. 137 (1872); *McMahon v. Macy*, 51 Id. 155 (1872); *Wheeler v. Millar*, 24 Hun, 541 (1881); s. c. affirmed, 90 N. Y. 353 (1882); *Stephens v. Fox*, 83 Id. 313 (1881).

In some of these cases it will be found that there is a disposition to make the judgment only *prima facie* evidence against the shareholder. In one or two cases even that is denied. Upon the whole, it may be said that the law in New York upon this point is unsettled, with perhaps a tendency, to be observed in the latest cases, to coincide with the other courts of the country.

⁴ *Keystone Bridge Co. v. Barstow*, 8 Mo. App. 494 (1880). Many of those de-

§ 211. *Contribution*.—Corporate creditors compelling stockholders to pay their subscriptions are under no obligation to see that the payments made by the subscribers are proportionally equal.¹ A court of chancery will compel subscribers to pay in full the amount of their unpaid subscriptions if the corporate indebtedness make it necessary, leaving them to seek contribution from the other shareholders.² The rule, moreover, is well settled that a shareholder who has been compelled to pay more than his proportion of the debts of the company may maintain an action against his co-stockholders for contribution.³

fenses are specified and treated of in full in Chapter X. As will be seen in Chapter IX, the defense of fraud inducing the subscription is no defense as against corporate creditors. So also fraud and mismanagement on the part of the directors and corporate officers is not a valid defense herein. *In re Republic Insurance Co.*, 3 Bias. 452 (1873).

Neither can the subscriber set up that the corporation, when his subscription was made, had no stock to offer. He is estopped by the subscription of his name in the corporation books. *Lathrop v. Kneeland*, 46 Barb. 432 (1866). *Cf. Mackley's Case*, L. R. 1 Chan. 247 (1875). Acts that estop the subscriber as against the corporation estop him as to corporate creditors. *Griswold v. Seligman*, 72 Mo. 110 (1880). But mere entries in corporate books are not sufficient to operate an estoppel. *Neilson v. Crawford*, 52 Cal. 248 (1877).

Where a firm or partnership becomes a subscriber in the copartnership name, corporate creditors may have execution against any one of the partners. The partnership subscription is not a defense of which any single partner can avail himself to escape liability. *Bray's Admr. v. Seligman's Admr.*, 75 Mo. 31 (1881). It is no defense that judgment against the defendant stockholder for the full amount of his liability, has been recovered by other creditors, and that he settled the same at a discount. *Kunkelman v. Reutcher*, 15 Brad. (Ill.) 271 (1884). Prominent among these is the defense that the corporation contracted with the defendant that his stock should be deemed fully paid up stock, although in fact the full par value had never been paid. *Vide Chapter III.*

The unpaid subscription may be collected in payment of damages for a tort

the same as for a contract debt. In Maine this rule is declared by statute. *Grindle v. Stone*, 4 East. Rep. 623 (1886).

¹ *Pentz v. Hawley*, 1 Barb. Chan. 122 (1845).

² *Pentz v. Hawley*, *supra*; *Evans v. Coventry*, 25 L. J. Chan. 489 (1856); *Marsh v. Burroughs*, 1 Woods. 463 (1871). Solvent stockholders are required to make up, for the benefit of creditors, the deficiency of defaulting or insolvent subscribers, to the full amount of the former's own unpaid subscriptions. *South Carolina Manufacturing Co. v. Bank of South Carolina*, 6 Rich. (Eq.) 227 (1854). But actual subscribers are not liable for that part of the capital stock which was never subscribed. *Evans v. Coventry*, 25 L. J. Chan. 489 (1856). It is no defense to show that notes were given in payment of subscriptions, or that the notes by insolvent persons were procured to be given, when it appears that nothing was ever realized from the notes. *Nathan v. Whitlock*, 9 Paige Chan. 152 (1841).

³ *Wincock v. Turpin*, 96 Ill. 135 (1880); *Meisser v. Thompson*, 9 Bradw. (Ill.) 368 (1881); *s. c. sub nom. Thompson v. Meisser*, 108 Ill. 359; *Millaudon v. New Orleans, &c., R. R. Co.*, 3 Rob. (La.) 488 (1843); *Marsh v. Burroughs*, 1 Woods, 463 (1871); *Holmes v. Sherwood*, 3 McCrary, 405 (1881); *Umsted v. Baskirk*, 17 Ohio St. 113 (1866); *Matthews v. Albert*, 24 Md. 527 (1866); *Stewart v. Lay*, 45 Iowa, 604 (1877); *Hadley v. Russell*, 40 N. H. 109 (1860); *Erickson v. Nesmith*, 46 Id. 371 (1866); *Masters v. Rossie Lead Mining Co.*, 2 Sandf. Chan. 301 (1845); *Slee v. Bloom*, 19 Johns. 456 (1822); *Aspinwall v. Torrence*, 1 Lans. 391 (1870); *Stover v. Flack*, 30 N. Y. 64 (1864); *Farrow v. Bivings*, 13 Rich. (Eq.) 25 (1866); *Middletown Bank v. Magill*, 5 Conn. 28, 61 (1823); *Brinham v. Wellersburg Coal*

Contribution may properly be enforced in the corporate creditor's suit. It is largely for this purpose that all the delinquent shareholders may be and should be made parties defendant.¹

Co., 47 Penn. St. 43 (1864). *Cf.* Andrews v. Collender, 13 Pick. 484 (1833); Gray v. Coffin, 9 Cush. 192 (1852); Sutton's Case, 3 De G. & Sm. 262 (1850). In Pennsylvania the right to contribution is said to be purely statutory. Brinham v. Wellersburg Coal Co., *supra*.

¹ N. Y. Code of Civil Procedure, §§ 1791-1794; Masters v. Rossie Lead Mining Co., 2 Sandf. Chan. 301 (1845); Holmes v. Sherwood, 3 McCrary, 405 (1881); Hadley v. Russell, 40 N. H. 109 (1860); Umsted v. Buskirk, 17 Ohio St. 113 (1866); Hodges v. Silver Hill Mining Co., 9 Oregon, 200 (1881).

Where the articles of incorporation provide that the indebtedness shall not exceed a certain sum, but debts are contracted in excess of the limit, and, the corporation being insolvent, the officer who contracted the debt pays it off out of his own individual funds, he cannot claim contribution unless the debt in excess of the limit was contracted by the unanimous assent of the stockholders. Haldeman v. Ainslie, Ky. (1884). The proceeding to enforce contribution must be in equity; it cannot be at law. Thompson v. Meisser, 108 Ill. 359 (1884).

CHAPTER XII.

STATUTORY LIABILITY OF STOCKHOLDERS TO CREDITORS.

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| <p>§ 212. Statutory liability in general.</p> <p>213. May be imposed by State constitution or by statute.</p> <p>214. The statutes to be strictly construed.</p> <p>215. Particular statutes construed.</p> <p>216. The statutory liability can be enforced by corporate creditors only.</p> <p>217. Waiver by corporate creditors of their statutory rights against shareholders.</p> <p>218-19. Enforcement of this statutory liability outside the State.</p> <p>220. Statutory liability not enforceable to pay damages recovered against the corporation in tort.</p> <p>221. Judgments, executions, &c., against the corporation, a condition prece-</p> | <p>dent to the right to enforce the statutory liability.</p> <p>§ 222. How far the judgment against the corporation is conclusive of the creditor's claims.</p> <p>223. Difficulty in determining whether the creditor's remedy is at law or in equity.</p> <p>224. Particular statutes considered as regards the creditor's remedy.</p> <p>225. The remedy at law, how far exclusive.</p> <p>226. Illustrations of the remedy in equity and at law.</p> <p>227. Stockholder's defenses against his statutory liability.</p> <p>228. Priority among creditors.</p> <p>229. Contribution among shareholders</p> |
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§ 212. *Statutory liability in general.*—Probably the most characteristic feature of a corporate existence is the fact that, by being a corporation, its stockholders are liable only for the par value of the stock held by them. This exemption from liability need not be declared in the charter, but flows from the very fact of incorporation. For this reason, legislatures are very careful, in giving joint-stock companies certain special powers, to distinctly declare that the company shall not thereby become a corporation. The very fact of incorporation by itself releases subscribers for stock from all liability for corporate debts, except to the extent of their unpaid subscriptions. It has been deemed wise, however, by the State legislature, in many instances, to increase the liability of stockholders to corporate creditors. Accordingly statutes are passed expressly declaring that the stockholders shall be so liable for a specified sum, in addition to their unpaid subscriptions. This is called the statutory liability of stockholders. It rarely if ever exists as regards stockholders in railroad corporations, but nearly always exists in the case of manufacturing and various other corporations.

§ 213. *May be imposed by State constitution or by statute.*—Many of the State constitutions contain provisions imposing a liability upon shareholders in corporation, in addition to the liability on their unpaid subscription.¹

Sometimes these constitutional provisions are not self-enforcing, but require legislation.² In the most cases, in fact, this additional liability of stockholders is enforced by the statute or act of the legislature.

The constitutionality of such statutes is generally unquestioned. Frequently, however, the statute is passed after the charter is granted. It then becomes a grave question whether or not the statute itself is constitutional. A full discussion,

¹ In Ohio (Const. of 1851, art. 13, § 3), and Kansas (Const. of 1859, art. 12, § 2), each stockholder is made liable, over and above his stock, in all cases, to a further sum equal in amount to such stock. In Kansas, railway, religious, and charitable are excepted. In Michigan (Const. of 1850, art. 15, § 7), each stockholder is individually liable for all labor performed for the corporation. In California (Const. of 1873, art. 12, § 3), the stockholder is individually and personally liable for such proportion of all debts and liabilities of the corporation, as his shares bear to the whole subscribed capital stock. In New York (Const. of 1846, art. 8, § 2), Indiana (Const. of 1851, art. 11, § 14), North Carolina (Const. of 1876, art. 8, § 2), Texas (Const. of 1876, art. 12, § 2), California (Const. of 1873, art. 12, § 2), South Carolina (Const. of 1868, art. 12, § 4), and in Alabama (Const. of 1875, art. 14), Nevada (Const. of 1864, art. 8), Missouri (Const. of 1875, art. 12), and Ohio (Const. of 1851, art. 13), there are constitutional provisions that dues from corporations or their stockholders are to be secured in a manner provided by law. In South Carolina (Const. of 1868, art. 12, § 5), stockholders are personally liable under fixed limitations. In Illinois (Const. of 1870, art. 11, § 6), Indiana (Const. of 1851, art. 11, § 6), Iowa (Const. of 1857, art. 8, § 9), Nebraska (Const. of 1875, art. 13, § 7), New York (Const. of 1846, art. 8, § 7), and West Virginia (Const. of 1872, art. 11, § 6), stockholders in banks are individually liable for the bank's debts, over and above their stock, to the amount of the stock held by them. In

Minnesota, to double the amount of their stock (Const. of 1857, art. 9, § 13). In Michigan (Const. of 1850, art. 15, § 3), stockholders in banks issuing money are liable for all the debts of the bank contracted while they are officers or such stockholders, each for his proportion, according to the amount of stock owned by him. But in Maryland (Const. of 1867, art. 3, § 39), and South Carolina (Const. of 1868, art. 12, § 6), they are liable only to the amount of their stock. In Alabama (Const. of 1875, art. 14, § 8), Missouri (Const. of 1875, art. 12, § 9), Nebraska (Const. of 1875, art. 13, § 4), Oregon (Const. of 1857, art. 11, § 3), and West Virginia (Const. of 1872, art. 11, § 2), there are constitutional provisions that stockholders shall in no case be liable otherwise than for unpaid stock owned by them. In Minnesota (Const. of 1857, art. 10, § 3), and Mississippi (Const. of 1869, art. 12, § 17), each stockholder is by the constitution liable for the amount of stock held or owned by him. In Minnesota shareholders in mechanical or manufacturing corporations are excepted. In Nevada (Const. of 1864, art. 8, § 3), it is enacted that stockholders shall not be individually liable for the debts and liabilities of the corporation.

² As, for example, the provision that "dues from corporations shall be secured by individual liability of the stockholders to an additional amount equal to the stock owned by each stockholder, and such other means as shall be provided by law." *Morley v. Thayer*, 3 Fed. Rep. 737 (1880).

however, of the principle of constitutional law as affecting stockholders is discussed elsewhere.¹

§ 214. *These statutes to be strictly construed.*—Inasmuch as all statutes creating an additional liability on the part of stockholders are in derogation of the common law, they are to be strictly construed. They are a wide departure from established rules, and, although founded on considerations of public policy and general convenience, are not to be extended beyond the plain intendment of the words of the statute.²

§ 215. *Particular statutes construed.*—The character, nature, and extent of the liability imposed by constitutional provisions, or by statute, upon stockholders, in addition to their common law liability, vary, of course, very widely, and the extent of the liability created by each statute will depend entirely upon the particular words of the enactment.³ There are, however, certain provisions

¹ See Chapter on Amendments and Constitutionality thereof.

² *O'Reilly v. Bard*, 105 Penn. St. 569 (1884); *Chase v. Lord*, 77 N. Y. 1 (1879); *Mean's Appeal*, 85 Penn. St. 75 (1877); *Gray v. Coffin*, 9 Cush. 192 (1852); *Dane v. Dane Manfg. Co.* 14 Gray, 489 (1859); *Chamberlin v. Huguenot Manfg. Co.* 118 Mass. 532 (1875); *Grose v. Hilt*, 36 Me. 22 (1853); *Coffin v. Rich*, 45 Id. 511; *Windham Provident Institution, &c. v. Sprague*, 43 Vt. 502 (1871); *Dauchy v. Brown*, 24 Id. 197; *Moyer v. Pennsylvania Slate Co.* 71 Penn. St. 293 (1872); *Youghiogeny Shaft Co. v. Evans*, 72 Id. 331 (1872); *Diven v. Lee*, 35 N. Y. 302 (1867); *Lowry v. Inman*, 46 Id. 119 (1871); *Salt Lake City National Bank v. Hendrickson*, 40 N. J. Law, 52. *Cf. Priest v. Essex Hat Manfg. Co.* 115 Mass. 380 (1874); *Ripley v. Sampson*, 10 Pick. 371 (1830); *Knowlton v. Ackley*, 8 Cush. 93 (1851); *Bassett v. St. Albans Hotel Co.*, 47 Vt. 313 (1875); *Davidson v. Rankin*, 34 Cal. 503 (1868); *Mokelumne Hill, &c., Co. v. Woodbury*, 14 Id. 265.

In the recent case of *Dewey v. St. Albans Trust Company*, 57 Vt. 332 (1885); a charter provision that, "If at any time the capital stock . . . shall be impaired by losses, or otherwise, the directors shall forthwith repair the same by assessment," was held not to impose a personal liability upon the stockholders of the corporation. The court proceeded

upon the theory that in construing such an enactment it is the duty of the courts to ascertain and carry out the intention of the legislature. All such statutes are to be construed according to the particular clauses found in them, and since these clauses vary widely in their formation, it would lead only to confusion to attempt to review the many statutory provisions on the liability of stockholders. *Carver v. Braintree Manfg. Co.*, 2 Story, 433, 447 (1843); *Bohn v. Brown*, 33 Mich. 257 (1876); *Lane v. Morris*, 8 Ga. 468, 475 (1850); *Ingalls v. Cole*, 47 Me. 530. *Cf. Chase v. Lord*, 77 N. Y. 1; *Moyer v. Pennsylvania Slate Co.*, 71 Penn. St. 293; *Potter v. Stevens Machine Co.*, 127 Mass. 592; *Dane v. Dane Manfg. Co.*, 14 Gray, 489; *Gray v. Coffin*, 9 Cush. 192.

It has been held that these statutes, being from one point of view contracts, are to be interpreted in the same way as any other contract containing like provisions. *Hicks v. Burns*, 38 N. H. 141 (1859).

It has also been held that, being remedial in their nature, they are, therefore, to be liberally construed. *Carver v. Braintree Manfg. Co.*, 2 Story, 433 (1843), by Mr. Justice Story; *Freeland v. McCullough*, 1 Denio, 413 (1845). But this, as it appears, is not the prevailing view.

³ *Bingham v. Rusting*, 5 Ala. 403 (1843); *Bank of St. Mary's v. St. John*,

imposing this additional liability which are found, in essentially the same form, in the constitution or statutes of very many of the States. Thus, the New York statute providing for the incorporation of manufacturing companies, passed in 1848,¹ has been copied, in its essential features, in almost every State in the Union. That statute contains a provision imposing a contingent statutory liability upon stockholders which has also been very generally reenacted in other States. By this provision stockholders in a manufacturing corporation are severally individually liable to corporate creditors to an amount equal to their stock until the whole capital stock is paid in, and a certificate to that effect is duly filed.² Stockholders in a national bank are subject to a personal liability.³

Sometimes the shareholder is made individually liable for

25 Id. 566, 620 (1854); *Smith v. Huckabee*, 53 Id. 191 (1875); *Lane v. Morris*, 8 Ga. 468 (1850); *Shaw v. Boylan*, 16 Ind. 384 (1861); *Trustees, &c. v. Flint*, 13 Metc. 539 (1847); *Coffin v. Rich*, 45 Me. 507 (1858); *Sumner v. Marcy*, 3 Woodb. & M. 105 (1847). •

¹ New York Session Laws, 1848, ch. 40.

² This liability, on the part of stockholders, "to an amount equal to their stock," is, it is believed, universally construed to be a liability in addition to and equal to the liability on the subscription, so that, when enforced and collected, each subscriber will have paid double for his stock, once on the subscription, and once on the statutory liability. *Matter of the Empire City Bank*, 18 N. Y. 199, 218 (1858); *Ohio Life Insurance Co. v. Merchants Ins. Co.*, 11 Humph. (Tenn.) 1 (1850); *Lewis v. St. Charles Co.*, 5 Mo. App. 225 (1878); *Wheeler v. Millar*, 90 N. Y. 353, 359 (1882); *South & Jones on Manfg. & Business Corp.*, § 100. *Cf. Briggs v. Penniman*, 8 Cow. 387; *Bank of Poughkeepsie v. Ibbotson*, 24 Wend. 473.

The stockholders' liability under this act is not confined to the original capital stock, but attaches on an increase of the capital, as authorized by the act, to such increased capital. Where, however, the original capital is paid in, in full, and a certificate made and recorded, the liability of the stockholders thus far is ended, and cannot be revived by an increase of the capital stock. The holders of the original stock will not, therefore, be lia-

ble thereon because of a failure to pay in the increased capital; that liability rests solely upon the holders of the increased stock, and is limited by the par value of such stock. *Veeder v. Mudgett*, 95 N. Y. 295 (1884). *Cf. Chubb v. Upton*, 65 U. S. 665 (1877). See also *Ochiltree v. Railroad Co.*, 21 Wall. 249 (1874); *Robinson v. Bank of Darien*, 18 Ga., 65, 87 (1855). *Cf. Woodruff v. Trapnall*, 10 How. 190, 206 (1850).

But a statutory liability cannot be reduced, and the rights of creditors thereby impaired, by reducing the par value of the shares. *Dane v. Young*, 61 Me. 160 (1872). See also Chapter on Amendments of Charter.

³ Thus stockholders in national banks are liable individually as follows (Rev. Stat. § 5151): "The shareholders of every national banking association shall be held individually responsible, equally and ratably, and not one for another, for all contracts, debts, and engagements of such association to the extent of the amount of their stock therein, at the par value thereof, in addition to the amount invested in such shares."

Stockholders in banking corporations in New York, other than national banks, are not liable individually for its debts (Laws 1838, ch. 260, § 23): "No shareholder of any such association shall be liable in his individual capacity for any contract, debt, or engagement of such association, unless the articles of association by him signed shall have declared that the shareholder shall be so liable." See *Sherman v. Smith*, 1 Black, 587, rela

certain classes of corporate indebtedness only, or for debts incurred for labor and supplies.¹ Such provisions are found in the statutory or constitutional law of nearly all of the States.² When shareholders are made liable by statute, absolutely or as partners, or in any way for the claims of those who are the servants or apprentices or laborers of the corporation, the question at once arises, when it is attempted to enforce that liability, whether or not the plaintiff comes within the prescribed class, that is to say whether he is a servant.³ And in all cases of a statutory

tive to the amendment as regards State banks issuing notes.

¹ *Weiss v. Mauch Chunk Iron Co.*, 58 Penn. St. 295 (1868); *Reading Industrial Manfg. Co. v. Graeff*, 64 Id. 395 (1870); *Moyer v. Pennsylvania Slate Co.*, 71 Id. 293 (1872); *Weigley v. Coal Oil Co.*, 5 Phila. 67 (1862).

² N. Y. Session Laws, 1848, ch. 40, § 18; N. Y. Session Laws, 1850, ch. 140, § 10; Mich. Const. of 1850, art. 15, § 7. See *Wakefield v. Fargo*, 90 N. Y. 213 (1882).

³ It may be stated, as the general rule, that only those who perform menial or manual services are within the class contemplated in the statute; "that he who performs them must be of a class whose members usually look to the reward of a day's labor or service for immediate or present support, from whom the company does not expect credit, and to whom its future ability to pay is of no consequence." *Wakefield v. Fargo*, 90 N. Y. 213, 217 (1882). Cf. *Williamson v. Wadsworth*, 49 Barb. 294; *Adams v. Goodrich*, 55 Ga. 335. This overrules some of the earlier New York cases, *e. g.* *Vincent v. Bramford*, 1 Jones & Sp. 506; *a. c.* 12 Abb. Prac. (N. S.) 252, which held an engineer and fireman, who sometimes also acted as superintendent, to be a servant within the meaning of the rule. *Harris v. Norvell*, 1 Abb. N. C. 127, which held a reporter employed by a newspaper company, and a city or assistant editor, if not an officer of the company, to be a servant. *Hovey v. Ten Broeck*, 3 Robertson, 316 (1865), holding an overseer and book-keeper within the protection of the act. In accordance with this interpretation of the act, the following employees have been held not servants or laborers within the protection of the rule:—The secretary of a manufacturing company, *Coffin v. Reynolds*, 87 N. Y. (640) 1868, overruling *Richard-*

son v. Abendroth, 43 Barb. 163, and perhaps *Williamson v. Wadsworth*, 49 Id. 294, which is the case of a civil engineer and traveling agent at a fixed salary.—A civil engineer, *Pennsylvania, &c., R. Co. v. Leuffer*, 84 Penn. St. 168 (1877). *Contra*, *Conant v. Van Schaick*, 24 Barb. 87. Cf. *Williamson v. Wadsworth*, 49 Barb. 294.—A consulting engineer, *Ericsson v. Brown*, 38 Barb. 390 (1862).—An assistant chief engineer, *Brockway v. Innes*, 39 Mich. 47 (1878). Cf. *Peck v. Miller*, 39 Mich. 594 (1878).—An overseer on a plantation, *Whitaker v. Smith*, 84 N. C. 340 (1879). *Contra*, *Hovey v. Ten Broeck*, 3 Robertson (N. Y. Super. Ct.) 316 (1875).—A contractor, *Boutwell Townsend*, 37 Barb. 205 (1860); *Aikin v. Wasson*, 24 N. Y. 482 (1862); *Balch v. New York, &c., R. R. Co.*, 46 Id. 521 (1871); *Atcherson v. Troy, &c., R. R. Co.*, 6 Abb. Prac. (N. S.) 329. Cf. *Kent v. New York, &c., R. R. Co.*, 12 N. Y. 628 (1855); *McCluskey v. Cromwell*, 11 Id. 593 (1854).—An agent of a mining corporation employed to take charge of its mines in a foreign country, *Hill v. Spencer*, 61 N. Y. 274 (1874); *Dean v. DeWolf*, 16 Hun, 186 (1878); *Krauser v. Ruckel*, 17 Id. 463 (1879).—A book-keeper and general manager, *Wakefield v. Fargo*, 90 N. Y. 213 (1882).—A superintendent, *Kincaid v. Dwinelle*, 59 N. Y. 548 (1875). Cf. *Gordon v. Jennings*, L. R., 9 Q. B. Div. 45. And compare, also, *Gurney v. Atlantic, &c., Ry. Co.*, 58 N. Y. 358 (1874). But in general only manual or menial laborers are protected by the statute. *Adams v. Goodrich*, 55 Ga. 335. Cf. *Heebner v. Chave*, 5 Penn. St. 115 (1847); *Harrod v. Hamer*, 32 Wis. 162 (1873); *Southworth & Jones on Manfg. & Business Corporations*, § 96. Under the mechanics' lien laws of the several States, a wider meaning has been given to the word "laborers." These cases are frequently confused with the statutes

liability, the extent of that liability will depend largely on the words used in the statute.¹ Where the stockholders are made liable "to double the amount of the stock held by them," each stockholder will be held liable once on his subscription, and once again under the statute.² And stockholders cannot, to any degree or by any means, limit their statutory liability to creditors,³ except by an express contract with creditors before the debt is contracted.

§ 216. *The statutory liability can be enforced by corporate creditors only.*—The statutory liability of the stockholder is created exclusively for the benefit of corporate creditors. It is not to be numbered among the assets of the corporation, and the corporation has no right or interest in it. It cannot enforce it by an assessment upon the shareholders.⁴ Nor can the corporation upon the insolvency assign it to a trustee for the benefit of creditors.⁵ It is a liability existing directly and immediately from the shareholders to the corporate creditors.⁶ Accordingly a

considered herein. *Stryker v. Cassidy*, 76 N. Y. 50 (1879); *Mutual Benefit Ins. Co. v. Rowood*, 26 N. J. Eq. 389; *Bank of Pennsylvania v. Gries*, 35 Penn. St. 423; *Arnoldi v. Gonin*, 22 Grant's Chan. (Upp. Can.) 314; *Mulligan v. Mulligan*, 18 La. Ann. 21; *Knight v. Norris*, 13 Minn. 475; *Raeder v. Bensberg*, 6 Mo. App. 445; *Foushee v. Grigsby*, 12 Bush, 75; *Smallhouse v. Kentucky, &c., Co.*, 2 Montana, 443; *Capron v. Stout*, 11 Nev. 304. The mere fact that one does some manual labor incidental to his position as manager, or foreman, or superintendent, will not constitute him a laborer within the intent of these statutes. *Krauser v. Ruckel*, 17 Hun, 463 (1879); *Ericsson v. Brown*, 38 Barb. 390. *Cf. Wakefield v. Fargo*, 90 N. Y. 213 (1882). But where a foreman did so much manual labor that it was not a mere incident of his foremanship, it was held that he might recover as a laborer. *Short v. Medberry*, 29 Hun, 39 (1883).

¹ In Massachusetts stockholders in manufacturing corporations are liable as tenants in common to creditors, to the extent of the capital stock, until it has been divided into shares. *Hawes v. Anglo Saxon Petroleum Co.*, 101 Mass. 385 (1869); *Id. v. Id.*, 111 Id. 200 (1872). *Cf. Burnape v. Haskins Steam Engine Co.*, 127 Mass. 586. But where some of the stock is held by the corporation itself this will not compel the other share-

holders to bear the statutory liability as to the stock so held by the corporation. *Crease v. Babcock*, 10 Metc. 525 (1846). And in Maryland the ordinary statutory liability, until the capital stock is paid in, makes the stockholder liable for unsubscribed shares. *Hager v. Cleveland*, 36 Md. 476 (1872). *Cf. Norris v. Johnson*, 34 Id. 485 (1871).

² *Perry v. Turner*, 55 Mo. 418 (1874); *Matthews v. Albert*, 24 Md. 527 (1866); *Norris v. Johnson*, 34 Id. 485 (1871); *Booth v. Campbell*, 37 Id. 522 (1872). But see *Schricker v. Ridings*, 65 Mo. 208 (1877); *Gay v. Keys*, 30 Ill. 413. A statute imposing a liability on stockholders to the amount of their subscriptions is not a statutory liability. The statute is only declaratory of the subscription liability. *Walker v. Lewis*, 49 Texas, 123.

³ *Union Mutual Insurance Co. v. Frear Stone Manfg. Co.*, 97 Ill. 537 (1881); *Dane v. Young*, 61 Me. 160 (1872).

⁴ *Umsted v. Buskirk*, 17 Ohio St. 113 (1866); *Liberty Female College Association v. Watkins*, 70 Mo. 13 (1879).

⁵ *Wright v. McCormack*, 17 Ohio St. 86, 95 (1866); *Dutcher v. Marine National Bank*, 12 Blatchf. 435 (1875).

⁶ *Bristol v. Sanford*, 12 Blatchf. 341 (1874); *Lane v. Morris*, 8 Ga. 468 (1850). The creditors may control it as of their own right—may assign it *inter vivos*, or

receiver of an insolvent corporation, invested with "all the estate, property, and equitable interests" of the concern, has no power to enforce such a liability as this.¹ The action to enforce can be maintained only by the creditors themselves, in their own right and for their own benefit.²

§ 217. *Waiver by corporate creditors of their statutory rights against shareholders.*—A corporate creditor may, by express contract, when the debt is incurred, waive his right to collect from the stockholder debts which the corporation fails to pay.³ And the corporation in its contracts with third persons may, it is held in England, lawfully stipulate for the exemption of its members from the liability imposed upon them by statute in the event of the insolvency of the corporation.⁴

§ 218. *Enforcement of this statutory liability outside the State.*—When some or all of the stockholders of a corporation are non-residents of the State in which the corporation exists, the important question arises, when a statutory liability is sought to be enforced, whether the courts of one State will enforce such a liability created by the statute law of another State. The statutory liability can usually be enforced only in the courts of the State where the stockholders live, since jurisdiction cannot be obtained elsewhere unless the stockholder has property which may be attached, or can be served personally with process. The question then arises, whether the courts of one State will enforce a statutory stockholder's liability created by the laws of another State. It is

transmit it to their personal representatives. *Pfohl v. Simpson*, 74 N. Y. 137 (1878); *Weeks v. Love*, 50 Id. 568 (1872). See also *Zabriskie v. Smith*, 13 Id. 322 (1855); *Wade v. Kalbfleisch*, 58 Id. 282 (1874); *Jackson v. Daggett*, 24 Hun, 204 (1881).

¹ *Billings v. Robinson*, 94 N. Y. 415 (1884); *Farnsworth v. Wood*, 91 N. Y. 308 (1883); *Cuykendall v. Corning*, 88 Id. 129 (1882); *Arenz v. Weir*, 89 Ill. 25; *Jacobson v. Allen*, 20 Blatchf. 525; *Hanson v. Donkersley*, 37 Mich. 184; *Cutting v. Damerel*, 88 N. Y. 410 (1882). *Cf.* *Davis v. Gray*, 16 Wall. 203 (1872); *Attorney-General v. Guardian Mutual, &c., Ins. Co.*, 77 N. Y. 272 (1879).

² *Farnsworth v. Wood*, 91 N. Y. 308 (1883); *Weeks v. Love*, 50 Id. 568 (1872); *Pfohl v. Simpson*, 74 Id. 137 (1878). See also *Mason v. New York Silk, &c., Co.*,

27 Hun, 307 (1882); *Billings v. Trask*, 30 Id. 314 (1883). But under special statutes in New York trustees are vested with power to collect these claims on behalf of creditors. *Walker v. Crain*, 17 Barb. 128; *Story v. Furman*, 25 N. Y. 215; *Cuykendall v. Corning*, 88 N. Y. 129 (1882); *Herkimer Co. Bank v. Furman*, 17 Barb. 116; *Hurd v. Tallman*, 60 Id. 272.

³ *Robinson v. Bidwell*, 22 Cal. 379 (1863); *French v. Teschemaker*, 24 Id. 518 (1864); *Basshor v. Forbes*, 36 Md. 154 (1872); *Brown v. Eastern Slate Co.*, 134 Mass. 590.

⁴ *Re Athenæum, &c., Society*, 3 De G. & J. 660 (1859); *Halket v. Merchant Traders, &c., Association*, 13 Q. B. 960 (1849); *Durham's Case*, 4 Kay & J. 517 (1858). *Cf.* *Shelford on Joint Stock Companies* (2d London edition), 4.

a liability depending on the law of the domicile of the corporation.¹ When, therefore, the courts of one State are asked to enforce the extraordinary liability imposed upon shareholders by the statutes of another State, two essential considerations enter into the determination of the matter.

First, is the statutory liability itself a liability arising out of a contract, or is it a mere penalty? Second, are the remedies provided by the laws of the State where suit is sought to be brought, adequate to the just enforcement of the liability? Upon the first question the courts are now essentially agreed in holding that the statutory liability in these cases is not penal in its nature, but is a liability arising out of a contract.² Nevertheless, although this is

¹ *Payson v. Withers*, 5 Biss. 269 (1873); *Seymour v. Sturgess*, 26 N. Y. 134 (1862); *Merrick v. Van Santvoord*, 34 Id. 208 (1866); *McDonough v. Phelps*, 15 How. Prac. 372 (1856); *Ex parte Van Riper*, 20 Wend. 614 (1839). *Cf.* *Hill v. Beach*, 12 N. J. Eq. 31; *Nabob of Carnatic v. East India Co.*, 1 Vesey, 371; *Dutch West India Co. v. Henriquez*, 1 Strange, 612; *King of Spain v. Mullett*, 2 Bligh (N. S.), 3. And see also *Land Grant Ry., &c., Co. v. Coffee County*, 6 Kan. 254.

In *Bateman v. Service*, L. R. 6 App. Cas. 386 (1881), the ground is taken that a liability created by statute remains the same wherever the corporation may transact its business, or wherever the shareholders may happen to live, and that the fact of doing business in a foreign State does not subject the shareholders of the corporation to the operation of laws which create statutory liability in such foreign State. In accordance with this view it was held in Ohio, where a foreign corporation, without statutory liability of its stockholders, did business in Ohio, where the statutes prescribe a personal liability for stockholders in domestic corporations of similar character, that the shareholders of the foreign corporation are protected by the exemption they enjoy at home. *Second National Bank v. Hall*, 35 Ohio St. 158 (1878). *Cf.* *Jessup v. Carnegie*, 80 N. Y. 441 (1880).

² *Corning v. McCullough*, 1 N. Y. 47 (1847); s. c. 49 Am. Dec. 287; *Freeland v. McCullough*, 1 Denio, 414 (1845); s. c. 43 Am. Dec. 685; *Story v. Furman*, 25 N. Y. 214 (1862); *Jones v. Barlow*, 62 Id. 202 (1875); *Hawthorne v. Calef*, 2 Wall. 10, 22 (1864); *Hodgson v. Cheever*, 8 Mo. App. 321 (1880); *Manville v. Edgar*, 8 Id. 324 (1880); *Queenan v. Palmer*, 34 Alb. L.

J. 117 (Ill. 1886); *Norris v. Wrenschall*, 34 Md. 492 (1871); *Terry v. Calnan*, 13 S. C. 220 (1879); *Tinker v. Van Dyke*, 1 Flippin, 532; *Lowry v. Inman*, 46 N. Y. 119, 127 (1871); *Strong v. Wheaton*, 38 Barb. 625; *Brown v. Hitchcock*, 36 Ohio St. 678 (1879); *Hatch v. Burroughs*, 1 Woods, 443; *Flash v. Conn.*, 109 U. S. 371 (1883); *Nimick v. Mingo Iron Works*, 25 West Va. 184 (1884). *Cf.* *Woods v. Hicks*, 7 Lea (Tenn.), 40 (1881); *Lawler v. Burt*, 7 Ohio St. 340 (1857). The 12th section of the New York Manufacturing Companies Act, to the effect that the corporate officers shall be liable for the debts of the corporation, in case they fail to make an annual public report of the business of the corporation (Laws of 1848, ch. 40), is universally held to be penal in its character. *Chase v. Curtis*, 113 U. S. 452 (1884); *Stokes v. Stickney*, 96 N. Y. 323 (1884); *Pier v. Hanmore*, 86 Id. 95 (1881); *Pier v. George*, 86 Id. 613 (1881); *Veeder v. Baker*, 83 Id. 156 (1880); *Knox v. Baldwin*, 80 Id. 610 (1880); *Easterly v. Barber*, 65 Id. 252 (1875); *Wiles v. Suydam*, 64 Id. 173 (1876); *Merchants' Bank of New Haven v. Bliss*, 35 Id. 412 (1866). In the case of *New Haven, &c., Co. v. Linden Spring Co.*, 6 East. Rep. 663 (Mass. 1886), the court, in refusing to enforce a subscription made to a foreign corporation, without an express promise to pay, said: "That the statutes of a State do not operate extra-territorially, *proprio vigore*, will be conceded. How far they should be enforced beyond the limits of the State which has enacted them, must depend on several considerations, as whether any wrong or injury will be done to the citizens of the State in which they are sought to be enforced, whether the policy

true of the ordinary statutes imposing a statutory liability on stockholders, there are many instances in which it is clear that the statutes are highly penal and will not be enforced outside of the State creating them.¹ It is settled law that one State will not enforce the penal legislation of another State.² Consequently, it is a general rule that the courts of one State will enforce a statutory liability of stockholders created in another State, only when that liability is held to have arisen from contract. If it is penal it can never be enforced out of the State by which it is created.³ A statutory liability, when it is a liability in contract, and not a penalty, may, under the proper limitations, be enforced in an action in the Federal courts.⁴

of its own laws will be contravened or impaired, and whether its courts are capable of doing complete justice to those liable to be affected by their decrees."

¹ Thus, for example, statutes that create liability because of failure on the part of corporate authorities to give certain specified notices, or to make certain reports, or because certain forbidden contracts are entered into by the corporation, are essentially penal in their nature, and cannot be enforced out of the State. In the following cases it appears that the courts of one State have refused to enforce a statutory liability imposed by another State, upon the general ground that the statutes were penal. *Cable v. McCune*, 26 Mo. 371 (1858); *Kritzer v. Woodson*, 19 Id. 327 (1854); *Lawler v. Burt*, 7 Ohio St. 340 (1857); *Sturges v. Burton*, 8 Id. 215 (1858); *Derrickson v. Smith*, 27 N. J. Law, 166 (1858); *First National Bank v. Price*, 33 Md. 487 (1870); *Halsey v. McLean*, 12 Allen, 438 (1866); *Hill v. Frazier*, 22 Penn. St. 320 (1853); *Harrisburgh Bank v. The Commonwealth*, 26 Id. 451 (1856); *Andrews v. Murray*, 33 Barb. 354 (1861); *Shaler, &c., Quarry Co. v. Bliss*, 34 Id. 309 (1861); *Bird v. Hayden*, 1 Robertson (N. Y. Super. Ct.), 383 (1863); *State v. John*, 5 Ohio, 217 (1831); *Scoville v. Canfield*, 14 Johns. 338 (1817); *United States v. Lathrop*, 17 Id. 4 (1819); *Gale v. Eastman*, 7 Metc. 14; *Steam Engine Co. v. Hubbard*, 101 U. S. 188 (1879); *Irwin v. McKean*, 23 Cal. 472; *Moier v. Sprague*, 9 R. I. 541. See *Cuykendall v. Corning*, 10 Fed. Rep. 342; *Cf. Ogden v. Folliot*, 3 Term Rep. 426 (1790); *Boughton v. Otis*, 21 N. Y. 261 (1860); *Losee v. Bullard*, 79 Id. 404 (1880); *Squires v. Brown*, 22 How. Prac.

35 (1860); *The Antelope*, 10 Wheaton, 66 (1825); *Western Transportation, &c., Co. v. Kilderhouse*, 87 N. Y. 430 (1882); *Lemmon v. The People*, 20 Id. 562 (1860). Moreover there can never be such a thing as a vested right to enforce a penalty. *Yeaton v. United States*, 5 Cranch, 281; *Norris v. Crocker*, 13 How. 429.

² Story on the Conflict of Laws, §§ 620, 621; Wharton on the Conflict of Laws, § 853 *et seq.*; Rorer on Interstate Laws, 148, 149, and the cases in the preceding note. "Penal laws are strictly local, and cannot have any operation beyond the jurisdiction of the country where they were enacted." *Scoville v. Canfield*, 14 Johns. 338 (1817).

³ See the cases in the three preceding notes. See also *Lowry v. Inman*, 46 N. Y. 119 (1871); *Patterson v. Baker*, 31 How. Prac. 180 (1867). *Cf. Union Iron Co. v. Pierce*, 4 Riss. 327 (1869); *Howell v. Manglesdorf*, 33 Kan. 194 (1885). When the Statute of Limitations is relied upon as a defense, it becomes material to settle whether the liability is of a penal nature or whether it arises *ex contractu*. In the former case the statute is generally short-er. *Vide* § 227, *infra*.

⁴ *Flash v. Conn*, 109 U. S. 371 (1883). And, in general, a creditor of a corporation whose shareholders are by statute made personally liable for its debts, may maintain a suit to enforce this liability wherever he can obtain jurisdiction over the necessary parties. The right to bring such an action, provided it does not seek to enforce a penalty, will not, it is believed, be denied in any State to the inhabitants of any other State, if there is jurisdiction of the proper parties defendant. *Aultman's Appeal*, 98 Penn. St. 505

§ 219. Upon the second question, that relating to the adequacy of the remedy or the procedure of the State in which the statutory liability is sought to be enforced, considerable difficulty is occasionally experienced. Where the statute imposing the liability prescribes the remedy, that remedy is held to be exclusive, and the effect of this sometimes is to prevent any enforcement of the liability except in the State creating it. When the statute creating the liability restricts its enforcement to a peculiar and unusual procedure, available only in the courts of the State in which the corporation exists, and making the procedure, as it were, as a part of the liability, such a liability sometimes cannot be enforced by the recognized procedure of another State.

In such a case the creditor can enforce the statutory liability only in the courts of the State where the corporation exists.¹ In general, the statutory liability of shareholders can be enforced in the courts of a foreign State, only by the employment of the remedies, and according to the course of procedure provided by the laws of that State.²

(1881); *Sackett's Harbor Bank v. Blake*, 3 Rich. Eq. 225; *Woods v. Hicks*, 7 Lea (Tenn.), 40 (1881); *First National Bank v. Price*, 33 Md. 487 (1870); *Ex parte Van Riper*, 20 Wend. 614 (1839); *McDonough v. Phelps*, 15 How. Prac. 372 (1856); *Lowry v. Inman*, 46 N. Y. 119 (1871); *Bank of Virginia v. Adams*, 1 Pars. Sel. Eq. Cas. 534 (1850). See also *Paine v. Stewart*, 33 Conn. 516 (1866); *Bond v. Appleton*, 8 Mass. 472 (1812); *Healy v. Root*, 31 Pick. 389 (1831); *Gale v. Eastman*, 7 Metc. 14 (1843); *Erickson v. Nesmith*, 15 Gray, 221 (1860); s. c. 4 Allen, 233 (1862); s. c. 46 N. H. 371 (1866); *Hutchins v. New England Coal Mining Co.*, 4 Allen, 580 (1862); *Halsey v. McLean*, 12 Id. 438 (1866); *Smith v. Mutual Life Insurance Co.*, 14 Id. 336 (1867); *Bateman v. Service*, L. R. 6 App. Cas. 386 (1881). And, when the suit is maintainable, the construction placed upon the statute of the State in which the corporation exists, by the courts of that State, is, as a general rule, controlling and will be followed by the courts of the State where the suit to enforce is brought. *Jessup v. Carnegie*, 80 N. Y. 441 (1880); *Chase v. Curtis*, 113 U. S. 452 (1884). See also *Hunt v. Hunt*, 72 N. Y. 236 (1878); *Fairfield v. County of Gallatin*, 100 U. S. 47 (1879); *Elmendorf v. Taylor*, 10 Wheaton, 152, 160; *Shelby v.*

Guy, 11 Id. 367; *Town of South Ottawa v. Perkins*, 94 U. S. 260, 267 (1876); *Peik v. Chicago, &c., R. R. Co.*, 94 Id. 164; *County of Leavenworth v. Barnes*, 94 Id. 70; *Adams v. Nashville*, 95 Id. 19, (1877); *Town of Elmwood v. Marcy*, 92 Id. 289 (1875).

¹ *Lowry v. Inman*, 46 N. Y. 119, 127 (1871); *Nimick v. Mingo Iron Works*, 25 West Va. 184 (1884). Thus where the statute provides that the creditor's remedy shall be by bill in equity, the liability cannot be enforced in a State which has no general system of equity jurisprudence and procedure. *Erickson v. Nesmith*, 4 Allen, 233 (1862); s. c. 15 Gray, 221 (1860). *Cf.* s. c. 46 N. H. 371 (1866). It should be noted here that, in Massachusetts, there is no general equity jurisdiction. The legislature, however, from time to time, has enlarged, by special acts, the power of the courts of that State, so that at present they have limited equity powers. In the case *Patterson v. Lynde*, 112 Ill. 196 (1884); s. c. 106 U. S. 519, the Illinois court refused to enforce the statutory liability of a stockholder in an Oregon corporation, where a single corporate creditor sought the enforcement. The Oregon procedure in equity was held to be his only remedy.

² *Drinkwater v. Portland Marine R. R. Co.*, 18 Me. 35 (1841); *Nimick v. Mingo*

§ 220. *Statutory liability not enforceable to pay damages recovered against the corporation in tort.*—The statutory liability imposed upon the shareholders in corporations is a liability, exclusively for debts and demands accruing against the corporation by reason of its contracts. It cannot, therefore, be enforced to pay damages recovered against the corporation in an action in tort.¹

§ 221. *Judgment, execution, &c., against the corporation, a condition precedent to the right to enforce the statutory liability.*—Even when not expressly provided by statute, it is the rule, according to the weight of authority, that corporate creditors, before they can proceed against the shareholders upon their statutory liability, must first exhaust their remedy against the corporation and its assets.² This rule is based upon the principle

Iron Works, 25 West Va. 184 (1884). *Cf.* Taft v. Ward, 106 Mass. 518 (1871). The validity, interpretation, and effect of the statute imposing the liability, are to be determined by the law of the State creating the corporation, but the remedy, the forms, and procedure to enforce the liability, must be governed by the law of the State where enforcement is sought. Lowry v. Inman, 46 N. Y. 119, 126 (1871). In New Hampshire, it is held to be necessary to set out in the pleading the remedy provided by the laws of the State creating the corporation and the liability, and to show that this remedy can be employed in the court where suit is brought. Rice v. Merrimack Hosiery Co., 56 N. H. 114 (1875).

¹ Heacock v. Sherman, 14 Wend. 59 (1835). In this case the stockholders in a company which owned a bridge, and against which a judgment had been recovered for damages, because the bridge was out of repair, were held not to be liable upon such a demand, since the act imposing a personal liability upon them contemplated a liability only for demands arising *ex contractu*. In general, the word "debt," as used in statutes imposing a personal liability upon stockholders, is construed to include only liabilities arising *ex contractu*, and not to include liability for damages recovered against the corporation in actions sounding in tort. Child v. Boston, &c., Iron Works, 137 Mass. 516 (1884); s. c. 50 Am. Rep. 328; Matter of the Boston, &c., Iron Works,

23 Fed. Rep. 880; Mill Dam Foundry Co. v. Hosey, 21 Pick. 417, 455 (1839); Dryden v. Kellogg, 2 Mo. App. 87 (1876); Doolittle v. Marsh, 11 Neb. 243; Esmond v. Bullard, 16 Hun. 65 (1878); s. c. affirmed, *sub nom.* Losse v. Bullard, 79 N. Y. 404 (1880); Archer v. Rose, 3 Brewster (Penn.), 264 (1871); Cable v. McCune, 26 Mo. 371 (1858); Bohn v. Brown, 33 Mich. 257, 263 (1876); Chase v. Curtis, 113 U. S. 452 (1884). *Cf.* Carver v. Braintree Mfg. Co., 2 Story, 432, 447; Wyman v. American Powder Co., 8 Cush. 168, 182; Gray v. Bennett, 3 Metc. 522; Chase v. Ingalls, 97 Mass. 524; Lowell v. Street Commissioners, 106 Id. 540; Zimmer v. Schleeauf, 115 Id. 52. Nor will the word "debt," in such enactments include a judgment for costs against the corporation in an action in tort. Schouton v. Kilmer, 8 How. Prac. 527 (1853); Lathrop v. Singer, 39 Barb. 396 (1863). But there is a contrary rule upon this point in Pennsylvania. Lane v. Baker, 2 Grant's Cases, 424 (1853).

² Mean's Appeal, 85 Penn. St. 75 (1877); Bayliss v. Swift, 40 Iowa, 648 (1875); McClaren v. Franciscus, 43 Mo. 452 (1869); Wright v. McCormack, 17 Ohio St. 86 (1866); Wehrman v. Reakirt, 1 Cinn. Super. Ct. 230 (1871); Lane v. Harris, 16 Ga. 217 (1854); Drinkwater v. Portland, &c., R. R. Co., 18 Me. 35; Dauchy v. Brown, 24 Vt. 197 (1852); Cambridge Water Works v. Somerville Dying Co., 4 Allen, 239 (1862); Toucey v. Bowen, 1 Biss. 81 (1855). *Cf.* Patter-

that the liability of the shareholder is not the primary resource of corporate creditors, and is not, therefore, to be resorted to if the assets of the corporation, including the assessments on the stock enforceable at common law, will suffice to pay the debts.¹ Frequently the statutes which impose this extraordinary or *extra* common law liability upon shareholders, provide that a creditor shall obtain judgment against the corporation, and that an execution duly levied thereunder shall have been returned wholly or partially unsatisfied, before the creditor has a right to proceed against the stockholder individually.² But in general, proceed-

son v. Wyomissing Mfg. Co., 40 Penn. St. 117 (1861); Harper v. Union Mfg. Co., 100 Ill. 225; Hatch v. Burroughs, 1 Woods, 439. The case Patterson v. Lynde, 112 Ill. 196 (1884), holds that the judgment must be obtained in the State where enforcement is sought, and that not even a judgment in the Federal Circuit Court for that district will suffice. Citing Steere v. Hoagland, 39 Ill. 264; McLune v. Benceni, 2 Ired. Eq. 513.

¹ Stewart v. Lay, 45 Iowa, 604 (1877); Wright v. McCormack, 17 Ohio St. 86 (1866). There is, however, a line of authorities in support of the proposition that a judgment against the corporation is not a prerequisite to the enforcement of the shareholders' statutory liability. Perkins v. Church, 31 Barb. 84 (1859); Southmayd v. Russ, 3 Conn. 52 (1819); Culver v. Third National Bank, 64 Ill. 528 (1871); Davidson v. Rankin, 34 Cal. 503 (1868); Young v. Rosenbaum, 39 Id. 646 (1870); Witherhead v. Allen, 4 Abb. App. Dec. 628 (1867); Manufacturing Co. v. Bradley, 105 U. S. 175 (1881); Morrow v. Superior Court, 64 Cal. 383 (1883); Bird v. Calvert, 22 S. C. 292 (1884). In these cases it is held in general, that the shareholder's liability under the statute is unconditional, original, and immediate, not dependent on the insufficiency of the corporate assets, and not collateral to that of the corporation upon the event of its insolvency. Thus, in the case of Manufacturing Company v. Bradley, 105 U. S. 175 (1881), it was held, that upon a bill being filed against the corporation, for the collection of a debt, the shareholders might properly be made parties, in order to avoid a multiplicity of suits, and upon the ground that the shareholders were immediately liable, under

that provision of their charter which made "members of the company . . . jointly and severally liable for all debts and contracts made by the company until the whole amount of the capital stock fixed and limited by the corporation" is paid in.

² See Laws of 1848, New York, chap. 40, § 24, commonly known as "The General Manufacturing Act." Handy v. Draper, 89 N. Y. 334 (1882); Southworth & Jones on Manuf. & Business Corporations, §§ 91, 121; Taylor on Corp., §§ 713, 724. See also Rocky Mountain National Bank v. Bliss, 89 N. Y. 338 (1882); Dean v. Mace, 19 Hun, 391 (1879). Sometimes there is a provision that the action must have been commenced by the creditor against the corporation within a given limited time after the maturity of the debt, in order to hold the shareowner on his statutory liability. N. Y. Laws of 1848, chap. 40, § 24; Shellington v. Howland, 53 N. Y. 371 (1873); Birmingham National Bank v. Mosser, 14 Hun, 605 (1878); Lindsley v. Simonds, 2 Abb. Prac. (N. S.) 69. Cf. State Savings Association v. Kellogg, 52 Mo. 583 (1873). And sometimes that a specified demand shall have been made. Haynes v. Brown, 36 N. H. 545 (1858). But even where the statute requires it, a suit to enforce a statutory liability need not be delayed until the corporate property has all been applied to the payment of debts, if it be clear that such property will be insufficient to pay everything. Munger v. Jacobson, 99 Ill. 349 (1881). Or where the corporation is clearly insolvent, and it would be idle to wait the return of the execution. Flash v. Conn., 109 U. S. 371 (1883). Cf. Toucey v. Bowen, 1 Biss. 81 (1855); Munger v. Jacobson, *supra*,

ings against the corporation are not to be required when they would be nugatory or impossible.¹

Where the statutes provide for an enforcement of the shareholder's statutory liability only upon the dissolution of the corporation, it is held that a dissolution, in the sense in which that term is here used, takes place when the corporation comes into the condition of having debts and no assets, or has ceased to act and exercise its corporate functions, or has suffered acts to be done which are subversive of the end and object for which it was created.²

§ 222. *How far the judgment against the corporation is conclusive of the creditor's claim.*—In general the judgment in these cases against the corporation is conclusive as to the amount and validity of the creditor's claim. Consequently when suit is brought to enforce the shareholder's statutory liability that judg-

or the corporation is dissolved. *Patterson v. Lynde*, 112 Ill. 196 (1884).

¹ *Shellington v. Howland*, 53 N. Y. 371 (1873); *State Sav. Ass. v. Kellogg*, 52 Mo. 583 (1873); *Dryden v. Kellogg*, 2 Mo. App. 87. Cf. *Ansonia Brass & Copper Co. v. New Lamp Chimney Co.*, 53 N. Y. 123 (1873); s. c. aff'd 91 U. S. 656 (1875); *Kincaid v. Dwinelle*, 59 N. Y. 548 (1875); *Birmingham National Bank v. Mosser*, 14 Hun, 605 (1878); *Hollingshead v. Woodward*, 35 Id. 410 (1885); *Paine v. Stewart*, 33 Conn. 516 (1866); *Chamberlin v. Huguenot Mfg. Co.*, 118 Mass. 532 (1875). In many of these cases it will appear that the National Bankruptcy Act is referred to, and that whenever, under the operation of this legislation, the performance of the conditions precedent to the due and regular enforcement of the liability of the shareholder under the State law, is rendered impossible, such performance is to be excused. So also where the property of the corporation is in the hands of a receiver, this does not in any way affect or qualify the right of the corporate creditors to enforce the remedy they have by statute against the shareholder individually. When the corporate assets are in the hands of a receiver, corporate creditors cannot, of course, maintain any action to appropriate the corporate property. But the statutory liability is not a corporate asset, and corporate creditors may, without reference to the receiver, prosecute their action freely, to recover from the

shareholders upon that ground. *Mason v. New York Silk Mfg. Co.*, 27 Hun, 307 (1882); *Jacobson v. Allen*, 12 Fed. Rep. 454 (1882). When the circumstances are such that the provisions of the statute in reference to the judgment against the corporation may properly apply, it is held in New York, that a proceeding *in rem*, and a judgment and execution therein, affecting only specific property of the corporation, is not sufficient. The proceeding and the judgment must be directly against the corporation. *Rocky Mountain National Bank v. Bliss*, 89 N. Y. 338 (1882); *Agate v. Edgar*, Genl. Term Com. Pleas, New York (not reported). Moreover, judgment and execution in a foreign State will not satisfy the requirement of the statute. It must be a judgment of a court of the State where the statutory liability is imposed and sought to be enforced, and the execution must duly issue out of a court of that State. *Dean v. Mace*, 19 Hun, 391 (1879); *Rocky, &c., Bk. v. Bliss*, *supra*; *Patterson v. Lynde*, 112 Ill. 196.

² *Bank of Poughkeepsie v. Ibbotson*, 24 Wend. 473 (1840); *Slee v. Bloom*, 19 Johns. 456 (1822); *Penniman v. Briggs*, Hopkins' Chan. 300 (1825); s. c. *sub nom.* *Briggs v. Penniman*, 8 Cowen, 387 (1826); *Morley v. Thayer*, 3 Fed. Rep. 737 (1880); *State Savings Association v. Kellogg*, 52 Mo. 583 (1873); *Dryden v. Kellogg*, 2 Mo. App. 87; *Perry v. Turner*, 55 Mo. 418 (1874); *Central Agric., &c., Association v. Alabama, &c., Ins. Co.*, 70 Ala. 120 (1881).

ment can be impeached only for fraud and collusion, or for want of jurisdiction. This, as will further appear, is not the rule in New York, but aside from the decisions of the courts of that State, the authorities are essentially agreed in sustaining this principle of law.¹ Sometimes the judgment is said to be only *prima facie* evidence of the creditor's claim.²

When the stockholders are, by statute, made liable for only a certain class of the corporate indebtedness, it is plain that they cannot be charged upon a judgment recovered against the corporation, unless it be shown that the claim in controversy comes within the class upon which they are liable.³

In New York, however, the view is taken that the statutory liability of stockholders makes them practically the guarantors of all debts contracted by the corporation. It devolves upon the creditor, accordingly, before he can enforce his claim against the shareholder individually, to show that the corporate assets are insufficient to satisfy his claim against it. The judgment against the corporation and the execution returned wholly or partially unsatisfied are, therefore, evidence only that the corporation cannot pay its debts. They only serve to show that the creditor has taken the necessary precedent steps to collect his claim from the corporate assets. But he cannot rely upon the judgment obtained against the corporation to establish his right to recover against the shareholder. It is not even *prima facie* evidence either of the amount or validity of his claim. The stockholder may set up any defense that the corporation might have set up.⁴

¹ *Thayer v. New England Lithographic Co.*, 108 Mass. 523 (1871); *Came v. Brigham*, 39 Me. 35 (1854); *Milliken v. Whitehouse*, 49 Id. 527 (1860); *Wilson v. The Stockholders, &c.*, 43 Penn. St. 424 (1862); *Donworth v. Coolbaugh*, 5 Iowa, 300 (1857); *Farnum v. Ballard, &c., Machine Shop*, 12 Cush. 507 (1853); *Robbins v. The Justices, &c.*, 12 Gray, 225 (1858); *Handrahan v. Cheshire Iron Works*, 4 Allen, 396 (1862); *Gaskill v. Dudley*, 6 Metc. 546; *Hampson v. Weare*, 4 Iowa, 13 (1856); *Bullock v. Kilgour*, 39 Ohio St. 543 (1883). *Cf. Merrill v. Suffolk Bank*, 31 Me. 57 (1849); *Holyoke Bank v. Goodman, &c., Manfg. Co.*, 9 Cush. 576 (1852); *Bank of Australasia v. Nias*, 16 Q. B. 717; s. c. 20 L. J. (C. B.) 284; *Connecticut River Savings Bank v. Fiske*, 60 N. H. 363; *Chesnut v. Pennell*, 92 Ill. 55.

² *Grund v. Tucker*, 5 Kan. 70 (1869); *Hawes v. Anglo-Saxon, &c., Co.*, 101 Mass. 385 (1869); *Grand Rapids Savings Bank v. Warren*, 52 Mich. 557; *Berger v. Williams*, 4 McLean, 577; *Merchants Bank v. Chandler*, 19 Wis. 435. And see *Neilson v. Crawford*, 52 Cal. 249.

³ *Bohn v. Brown*, 33 Mich. 257; *Wilson v. The Stockholders, &c.*, 43 Penn. St. 424; *Convent v. Van Schaick*, 24 Barb. 87. *Cf. Larrabee v. Baldwin*, 35 Cal. 155 (1868); *Farnsworth v. Wood*, 91 N. Y. 308 (1883).

⁴ *Moss v. McCullough*, 5 Hill, 131 (1843). [This case was reversed upon another point in *McCullough v. Moss*, 5 Denio, 567 (1846).] *McMahon v. Mazy*,

§ 223. *Difficulties in determining whether the creditor's remedy is at law or in equity.*—Perhaps the most difficult, unsettled, and unsatisfactory question concerning the statutory liability of stockholders is the question whether that liability must be enforced at law, or must be in equity, or may be in either a court of law or of equity. After determining this point there arises the further difficulty of ascertaining who shall be parties plaintiff and parties defendant; whether one corporate creditor may sue or all must join; whether one stockholder may be pursued as a single defendant or all the stockholders must be brought in. The law on these points is in a transition stage. The question is largely one of practice, and from experience the courts will doubtless evolve that rule which is most just and convenient. At present, however, not only must the decisions of the State in which the action is brought be examined, but it is necessary also to note carefully the wording of the statute creating the liability.¹ Sometimes the shareholder's liability is said to be like that of partners at common law—in other cases like that of sureties; again that it

51 N. Y. 155 (1872); *Miller v. White*, 50 Id. 137 (1872); *Chase v. Curtis*, 113 U. S. 452 (1884); *Esmond v. Bullard*, 16 Hun, 65 (1878). But see *Slee v. Bloom*, 20 Johns. 669 (1822); *Belmont v. Coleman*, 21 N. Y., 96 (1860); *Hastings v. Drew*, 76 Id. 9 (1879); *Stephens v. Fox*, 83 Id. 313 (1881), in which the ground is taken that the judgment in these cases is *prima facie* evidence or more, without, however, overruling the earlier cases. See also *Conant v. Van Schaick*, 24 Barb. 87 (1857); *Moss v. Oakley*, 12 Hill, 265 (1842), and *Trippe v. Huncheson*, 82 Ind. 307; *Southmayd v. Russ*, 3 Conn. 52 (1819) *Whitney Arms Company v. Barlow*, 63 N. Y. 62 (1875); *Chase v. Curtis*, 113 U. S. 452 (1884). Practically the corporate creditor must bring his action anew against the shareholder upon his original demand. *Bailey v. Bancker*, 3 Hill, 188 (1842); *Kincaid v. Dwinelle*, 59 N. Y. 548 (1875); *Moss v. Averell*, 10 Id. 449 (1853). As to the effect of recitals in a decree against the corporation, see *Chesnut v. Pennell*, 92 Ill. 55. This judgment against the corporation is admissible only as evidence that the condition precedent to his right to recover from the shareholder has been complied

with. *Wheeler v. Miller*, 24 Hun, 542 (1881); s. c. *sub nom. Wheeler v. Millar*, 90 N. Y. 353 (1882); *Strong v. Wheaton*, 38 Barb. 616. But *cf. Tyng v. Clarke*, 9 Hun, 269 (1876). See also *Bissitt v. Kentucky, &c., Navigation Co.*, 15 Fed. Rep. 353 (1882), and the annotation; *Union Bank v. Wando Mining, &c., Co.*, 17 S. C. 339 (1881). The judgment may avail, however, in these cases, to prevent the Statute of Limitations from barring the action. *Van Cott v. Van Brunt*, 2 Abb. N. C. 283, 294; *rev'd on other points*, 82 N. Y. 535.

¹ Mr. Chief Justice Waite, in *Terry v. Little*, 101 U. S. 216, 217 (1879), said: "The first thing to be determined in all such cases is, therefore, what liability has been created. There will always be difficulty in attempting to reconcile cases of this class, in which the general question of remedy has arisen, unless special attention is given to the precise language of the statute under consideration. The remedy must always be such as is appropriate to the liability to be enforced. The statute which creates the liability may declare the purposes of its creation and provide directly or indirectly a remedy for its enforcement."

is joint and several—or joint or several—sometimes at law and sometimes in equity.

§ 224. *Particular statutes considered as regards the creditor's remedy.*—Under a statute providing that “each shareholder shall be individually and personally liable for his proportion of all the debts and liabilities of the company contracted or incurred, . . . for the recovery of which joint or several actions may be prosecuted,” it has been held that the liability of the shareholders is substantially that of partners, and that all the stockholders must be joined as parties defendant.¹ So also a general joint and several liability for all the corporate debts makes the stockholders liable as partners as though there had been no incorporation.² Under the provisions of the constitution and statutes of Ohio, it is held that while the undertaking of the shareholder is not primary, and is to be resorted to only in case of the insolvency of the corporation, still the liability, when it does properly arise, is essentially that of partners.³ And, in general, unless the statute prescribes otherwise, the common law rules as to the liability of

¹ Mokelumne Hill Canal, &c., Co. v. Woodbury, 14 Cal. 265 (1859); Mitchell v. Beckman, 64 Id. 117 (1883); Davidson v. Rankin, 34 Id. 503 (1868); Young v. Rosenbaum, 39 Id. 646 (1870); Larrabee v. Baldwin, 35 Id. 155 (1868); McAuley v. Yorke Mining Co., 6 Id. 80 (1856); Adkins v. Thornton, 19 Ga. 325 (1856) [this case is frequently misquoted, owing to a misprint in the original report, as Dozier v. Thornton]; Branch v. Baker, 53 Ga. 502 (1874); Dane v. Young, 61 Me. 160 (1872); Castleman v. Holmes, 4 J. J. Marsh. 1 (1830). Cf. Morawetz on Corp. (2d edition), § 878; Taylor on Corp., § 718 *et seq.*; also § 726; Fuller v. Ledden, 87 Ill. 312; Brown v. Hitchcock, 36 Ohio St. 678.

² Planters Bank, &c. v. Bivingsville, &c., Manfg. Co., 10 Rich. Law, 95 (1856); Southmayd v. Russ, 3 Conn. 52 (1819); Middletown Bank v. Magill, 5 Id. 28, 45 (1823); Deming v. Bull, 10 Id. 409 (1835); Conant v. Van Schaick, 24 Barb. 87 (1857); Allen v. Sewall, 2 Wend. 327 (1829); Moss v. Oakley, 2 Hill, 265 (1842); Harger v. McCullough, 2 Denio, 119 (1846); McCullough v. Moss, 5 Id. 567 (1846); Corning v. McCullough, 1 N. Y. 47 (1847); Moss v. Averell, 10 Id. 449 (1833); Wiles v. Suydam, 64 Id. 173, 176 (1876); Conklin v. Furman, 8 Abb.

Prac. (N. S.) 164; s. c. 57 Barb. 487; Abbott v. Aspinwall, 25 Barb. 207; Erickson v. Nesmith, 46 N. H. 371 (1866); White v. Blum, 4 Neb. 555 (1876); New England Commercial Bank v. Newport Steam Factory, 6 R. I. 154 (1859); Moies v. Sprague, 9 Id. 541 (1870); Witherhead v. Allen, 28 Barb. 667; Chase v. Lord, 77 N. Y. 33; Jones v. Barlow, 62 Id. 210; Tinker v. Van Dyke, 1 Flippin, 532.

³ And that although the stated extent of the shareholder's liability, as provided by the statute, cannot be exceeded, still, up to the full measure of his liability, he may be charged, although it be shown that, if other solvent shareholders had contributed their full proportion, it would not be necessary for him to pay. Wehrman v. Reakirt, 1 Cinn. Super. Ct. 330 (1871); Brown v. Hitchcock, 36 Ohio St. 678. Cf. Stewart v. Lay, 45 Iowa, 604 (1877); Crease v. Babcock, 10 Mete. 525 (1846); Hodgson v. Cheever, 8 Mo. App. 321. In Wisconsin, stockholders in banking corporations are liable, by statute, as original and principal debtors, substantially as though they were partners, except, as in Ohio, that the responsibility of each is limited to a sum equal to his shares of stock. Coleman v. White, 14 Wis. 700 (1862); Carpenter v. Marine Bank, Id. 705, n.

partners, and the remedies for enforcing that liability apply to the statutory liability of shareowners in incorporated companies.¹ The question whether the statutory liability of the shareholder in any given case is that of a partner at common law, is one of very great practical importance, since, if the relation of the shareholders be that of partners, the corporate creditor may have his action at law against them as such to collect his debt. They are liable jointly or severally. Each is liable as a principal, and not as a surety, and each is liable for the whole corporate debt, not otherwise provided for, to the full extent of the statutory liability imposed upon his stock.² Where the statute provides expressly the form of the remedy in this respect, it is the well established rule that that remedy was intended by the legislature to exclude every other, and it must be strictly pursued.³

¹ *Story v. Furman*, 25 N. Y. 214 (1862); *New England Commercial Bank v. Newport Steam Factory*, 6 R. I. 154 (1859); *Moies v. Sprague*, 9 Id. 541 (1870). It is sometimes held that a general statutory liability means a liability on the part of the stockholder only in the proportion which his interest bears to the total indebtedness of the corporation. *Boyd v. Hall*, 56 Ga. 563 (1876); *Reynolds v. Feliciana Steamboat Co.*, 17 La. Rep. 397 (1841). In such a case, where the shareholders are jointly and severally personally liable for debts contracted by the corporation, which it cannot or does not pay, in proportion to the number of shares they own, it seems to be settled that they are to be held principal debtors, and not mere sureties for the corporation. *Harger v. McCullough*, 5 Denio, 119 (1846); *Corning v. McCullough*, 1 N. Y. 47 (1847); *Moss v. Averell*, 10 Id. 450 (1853); *Simonson v. Spencer*, 15 Wend. 548 (1836); *Bailey v. Bancker*, 3 Hill, 188 (1842); *Southmayd v. Russ*, 3 Conn. 52 (1819); *Marcy v. Clark*, 17 Mass. 330 (1821). In Michigan it is held that they are sureties. *Hanson v. Donkersley*, 37 Mich. 184. *Cf. Grand Rapids Savings Bank v. Warren*, 52 Id. 557. It has been held also that they are not sureties for each other. *Lane v. Harris*, 16 Ga. 217, 234 (1854); *Crease v. Babcock*, 10 Metc. 525 (1846). *Cf. Larrabee v. Baldwin*, 35 Cal. 155 (1868). This seems to be the rule, in general, as to all statutory liability. *Young v. Rosenbaum*, 39 Cal. 646 (1870); *Taylor on Corporations*, §§ 714, 715.

² *Erickson v. Nesmith*, 46 N. H. 371 (1866); *Thompson v. Meisser*, 108 Ill. 359. It is obvious that the question whether the creditor, in pursuing his remedy against the shareholder, may sue one or any of the shareholders at his option, or must sue all, in a joint action, is of the highest importance. It goes to the very form and essence and content of his action, but it is a point upon which, as has been already intimated, a text writer cannot deduce from the reported cases any clearly settled rule of general application. It is, in every case where the statute does not contain an explicit provision, a question of construction to be determined by the courts in expounding the words of the statute.

³ *Lowry v. Inman*, 46 N. Y. 119, 127 (1871); *Morley v. Thayer*, 3 Fed. Rep. 737, 741 (1880); *Haskins v. Harding*, 7 West. Junist, 622; *Allen v. Walsh*, 25 Minn. 543 (1879); *Windham Provident Savings Institution v. Sprague*, 43 Vt. 502 (1871); *Bassett v. St. Albans Hotel Co.*, 47 Id. 313 (1875); *Pollard v. Bailey*, 20 Wall. 520 (1874); *Knowlton v. Ackley*, 8 Cush. 93, 98 (1851); *Erickson v. Nesmith*, 15 Gray, 221 (1860); *Brinham v. Wellersburg Coal Co.*, 47 Penn. St. 43 (1864); *Hoard v. Wilcox*, 47 Id. 51; *Youghiogheny Shaft Co. v. Evans*, 72 Id. 331 (1872). *Cf. Andrews v. Callender*, 13 Pick. 484 (1833); *Potter v. Stevens Machine Co.*, 127 Mass. 592 (1879); *Groce v. Hilt*, 36 Me. 22 (1853); *Diven v. Lee*, 36 N. Y. 302 (1867); *Wehrman v. Reakirt*, 1 Cinn. Super. Ct. 230 (1871). In the greater number of cases it will be found

In New York the shareholders' liability, imposed by the statute known as the General Manufacturing Act,¹ is held to be individual, so that any creditor who has recovered a judgment against the company, and sued out an execution thereon, which has been returned unsatisfied, may sue any stockholder and recover to the extent provided by the statute in an action at law.² So elsewhere, when it is provided by statute that the shareholders "shall, to the amount of the stock by them held, be jointly and severally liable for all the debts and responsibilities of such company," it is held that an action at law may be maintained on the individual liability by any corporate creditor against any individual shareholder.³

that there are no similar charter or statutory provisions in point, by which the creditor can be guided in determining whether his action must be against all the shareholders or not. He will, therefore, depend upon the terms of the statute from which his right is derived and by which the liability is imposed, and upon the construction put upon that particular statute by the courts. *Jacobson v. Allen*, 12 Fed. Rep. 454 (1882); *Cuykendall v. Miles*, 10 Id. 342 (1882); *Terry v. Little*, 101 U. S. 216. In Illinois, under the charter provision that "each stockholder shall be liable to double the amount of stock" owned, it was held that the stockholders were severally and individually liable, that is that an action at law against one or all of them would lie. *McCarthy v. Lavasche*, 89 Ill. 270 (1878); *Hull v. Burtis*, 90 Id. 213 (1878); *Fuller v. Ledden*, 87 Id. 310; *Thebus v. Smiley*, 110 Id. 316; *Jacobson v. Allen*, 12 Fed. Rep. 454 (1882); s. c. 20 Blatchf. 525. In Illinois there was some doubt as to whether the bill in equity would lie, but the late case of *Tunesma v. Schuttler*, 114 Ill. 156 (1885), holds that in case the corporation is insolvent and the corporate creditors numerous, a bill in equity is the proper remedy. Under the Manufacturing Company's Act of Illinois, the creditor's remedy is held to be clearly in equity. *Rounds v. McCormick*, 114 Ill. 252 (1885); *Harper v. Union Mfg. Co.*, 110 Ill. 222; *Low v. Buchanan*, 94 Ill. 76. As regards the method of enforcement of the statutory liability of stockholders in national banks, see *Irons v. Manufacturers Natl. Bk.*, 27 Fed. Rep. 591 (1886); *Hobart v. Johnson*, 19 Blatch. 359 (1881); *Anderson v. Line*, 14 Fed. Rep. 405 (1880).

¹ New York Laws of 1848, chap. 40, §§ 10, 11, 24.

² *Abbott v. Aspinwall*, 26 Barb. 202 (1857); *Wiles v. Suydam*, 64 N. Y. 173 (1876); *Shellington v. Howland*, 53 Id. 371 (1873); *Handy v. Draper*, 89 Id. 334 (1882); *Rocky Mountain National Bank v. Bliss*, Id. 338 (1882); *Mathez v. Neidig*, 72 Id. 100 (1878); *Flash v. Conn.*, 109 U. S. 371, 380 (1883); *Southworth & Jones on Manufg. & Business Corporations*, § 107; *Weeks v. Love*, 50 N. Y. 588 (1872). And this was the rule also under the earlier statute of March 22, 1811. See 3 R. S. 282; *Bank of Poughkeepsie v. Ibbotson*, 24 Wend. 473 (1840); *Van Hook v. Whitlock*, 3 Paige, 409; *Simonson v. Spencer*, 15 Wend. 548 (1836). But when the action is to enforce the statutory liability to employees, "laborers, servants, and apprentices," in New York, it has been held that all the shareholders should be made parties. *Strong v. Wheaton*, 38 Barb. 616 (1861).

³ *Grund v. Tucker*, 5 Kan. 70 (1869); *Norris v. Johnson*, 34 Md. 485 (1871). See *Bullard v. Bell*, 1 Mason, 243 (by Story, J.). Cf. *Matthews v. Albert*, 24 Md. 527 (1866); *Culver v. Third National Bank*, 64 Ill. 528 (1871); *Bond v. Appleton*, 8 Mass. 472 (1812); *Harris v. First Parish in Dorchester*, 23 Pick. 112 (1839); *Coleman v. White*, 14 Wis. 700 (1862). Under a Georgia statute, by the provisions of which each shareholder in banking corporations in that State is made liable to redeem his proportionate share of the outstanding circulation, a single creditor may have his action at law against any individual shareholder. *Lane v. Harris*, 16 Ga. 217 (1854); *Lane v. Morris*, 8 Ga. 468 (1850); *Branch v. Baker*, 53 Id. 502 (1874); *Hatch v. Burroughs*, 1 Woods, 439 (1870). Cf. *Bank of Poughkeepsie v. Ibbotson*, 24 Wend. 473 (1840).

§ 225. *The remedy at law, how far exclusive.*—It will generally be found where an action at law can be maintained by any individual creditor against any individual stockholder, to enforce the statutory liability, that this is not held to be the creditor's exclusive remedy. The rule is believed, in general, to go no further than to allow such an action, leaving the further remedy by suit in equity, on behalf of all the creditors and against all the shareholders, to be pursued at the option of the creditors.

On the other hand, there is to be found a line of decisions which hold that while an action at law is a proper proceeding on the part of the corporate creditor, the liability of the shareholder is joint, and that in consequence all should be made parties defendant.¹

§ 226. *Illustrations of the remedy in equity and at law.*—The remedy in equity is the favorite remedy of the courts. Accordingly it is frequently held that an action at law to enforce a statutory liability is not a proper proceeding, but that the rights of all parties can be properly adjusted only in a court of equity, and that the latter remedy is exclusive of all others.²

¹ *Mansfield Iron Works v. Willcox*, 52 Penn. St. 377 (1866); *Brinham v. Wellersburg Coal Co.*, 47 Id. 43 (1864); *McHose v. Wheeler*, 45 Id. 32 (1863); *Hoard v. Wilcox*, 47 Id. 51 (1864). In Pennsylvania the corporation also should be made a party defendant. *Mansfield Iron Works v. Willcox*, 52 Penn. St. 377 (1866). *Cf. Deming v. Bull*, 10 Conn. 409 (1835); *Middletown Bank v. Magill*, 5 Id. 28 (1823). In Vermont a provision that shareholders "shall be personally holden," is held to create only a joint liability. *Windham Provident Savings Institution v. Sprague*, 43 Vt. 502 (1871).

² Thus, under a charter provision that stockholders shall "be bound respectively for all debts of the bank in proportion to their stock holden therein," it was held that an action at law by a single creditor against a single stockholder would not lie. *Pollard v. Bailey*, 20 Wall. 520 (1874); *Hatch v. Dana*, 101 U. S. 205 (1879); *Terry v. Little*, Id. 216. *Cf. Wright v. McCormack*, 17 Ohio St. 86 (1866); *Smith v. Huckabee*, 53 Ala. 191 (1875); *Sands v. Kimbark*, 37 Barb. 108, 120 (1863); *Cushman v. Shepard*, 4 Id. 113 (1848). Nor under a statute making the stockholders of a banking company

"individually responsible to the amount of their respective share or shares of stock for all its indebtedness and liabilities of every description." *Coleman v. White*, 14 Wis. 700 (1862); *Carpenter v. Marine Bank*, Id. 705, n.

Also upon the ground that at law the indebtedness of the corporation and the several liabilities of the members could not be equitably adjusted. See also *Allen v. Walsh*, 25 Minn. 543 (1879); *Jones v. Jarman*, 34 Ark. 323 (1879); *Low v. Buchanan*, 94 Ill. 76 (1879); and particularly *Flash v. Conn*, 109 U. S. 371 (1883); *Queenan v. Palmer*, 34 Alb. L. J. 117 (Ill., 1886). *Cf. Stewart v. Lay*, 45 Iowa, 604 (1877); *Norris v. Johnson*, 34 Md. 485 (1871); *Faymonville v. McCullough*, 59 Cal. 285 (1881); *Garrison v. Howe*, 17 N. Y. 458 (1858); *Story v. Furman*, 25 Id. 214 (1862).

Where, in South Carolina, the charter of the bank provided that upon the failure of the bank, "each stockholder shall be liable and held bound . . . for any sum not exceeding twice the amount of . . . his . . . shares," it was held by the Supreme Court of the United States that a suit in equity by or on behalf of all the creditors is the only appro-

It is uncertain whether a stockholder, who is also a creditor of the corporation, can bring an action at law against his co-stockholders to enforce a statutory liability. In Massachusetts¹ and New York² the rule is settled that such an action cannot be maintained. In those jurisdictions the only remedy for such a creditor in such a case is in a court of equity.

But in Pennsylvania³ and in Maine⁴ the rule is otherwise, and it is no objection to the creditor's action that he be, himself, also a shareholder.⁵ Where an action at law can be maintained, and the shareholder's liability is limited and several, each shareholder being made liable for a sum certain, a separate action will lie against each one.⁶ And unless the remedy at law has been enlarged by statute, so as to allow judgment separately against each one of several defendants before the court in the same proceeding, each creditor must sue each shareholder, or each creditor must sue some one or more shareholders separately.⁷ In many

priate mode of enforcing the liability incurred by such a failure. *Terry v. Little*, 101 U. S. 216 (1879).

¹ *Thayer v. Union Tool Co.*, 4 Gray, 75 (1855); *Potter v. Stevens Machine Co.*, 127 Mass. 592 (1879).

² *Bailey v. Bancker*, 3 Hill, 188 (1842); overruling upon this point *Simonson v. Spencer*, 15 Wend. 548 (1836); *Beers v. Waterbury*, 8 Bosw. 396 (1861); *Richardson v. Abendroth*, 43 Barb. 162 (1864). But see *contra*, *Sanborn v. Lefferts*, 58 N. Y. 179 (1874); *Garrison v. Howe*, 17 N. Y. 458 (1858). *Cf.* *Slee v. Bloom*, 5 Johns. Chan. 366, 382 (1821).

³ *Brinham v. Wellersburg Coal Co.*, 47 Penn. St. 43 (1864).

⁴ *Fowler v. Robinson*, 31 Me. 189 (1850).

⁵ In New York it seems that the assignee of a shareholder may bring the suit to enforce statutory liability. *Woodruff & Beach Iron Works v. Chittenden*, 4 Bosw. 406 (1859). See *Garrett v. Sayles*, 1 Fed. Rep. 371 (1880), to the point that an assignee in bankruptcy may maintain such a suit. But this is pointedly denied in Massachusetts, and, as it appears, upon tenable grounds. *Potter v. Stevens Machine Co.*, 127 Mass. 592 (1879). For if an assignee may sue, there is an end of the rule.

⁶ *Bank of Poughkeepsie v. Ibbotson*, 24 Wend. 473 (1840); *Perry v. Turner*, 55 Mo. 418 (1874); *Boyd v. Hall*, 56 Ga. 563 (1876); *Jones v. Wiltberger*, 42 Id.

575 (1871); *Lane v. Harris*, 16 Id. 217 (1854); *Paine v. Stewart*, 33 Conn. 516 (1866); *Culver v. Third National Bank*, 64 Ill. 528 (1871); *Abbott v. Aspinwall*, 26 Barb. 202 (1857); *Garrison v. Howe*, 17 N. Y. 458 (1858); *Terry v. Little*, 101 U. S. 216 (1879).

The late case of *Mason v. Alexander*, 13 Am. & Eng. Corp. Cas., 54 (O., 1886), holds that the corporation is a necessary party to the creditor's suit in equity, that judgment against the stockholders is to be against them severally, and that interest is to be allowed from the commencement of the suit, "although the amount of recovery may thereby exceed the stockholder's original liability."

⁷ *Bank of Poughkeepsie v. Ibbotson*, 24 Wend. 473; *Abbott v. Aspinwall*, 26 Barb. 202 (1857); *Pettibone v. McGraw*, 6 Mich. 441 (1859); *Paine v. Stewart*, 33 Conn. 516 (1866); *Matter of the Hollister Bank*, 27 N. Y. 393 (1863); *Perry v. Turner*, 55 Mo. 418 (1874). *Cf.* *Pratt v. Bacon*, 10 Pick. 122 (1830); *Milroy v. Spurr Mountain Iron Mining Co.*, 43 Mich. 231 (1880). But where the shareholder's liability is held to be like that of a partner, then all must be joined as defendants, and the omission of any one is ground for a plea in abatement. *Allen v. Sewall*, 2 Wend. 327 (1829); *Strong v. Wheaton*, 38 Barb. 616 (1861); *Reynolds v. Feliciana Steamboat Co.*, 17 La. Rep. 397 (1841); *Bonewitz v. Bank*, 41 Ohio St. 78. *Cf.* *Dodge v. Minnesota, &c.*,

jurisdictions the rule prevails that creditors in these cases have a concurrent remedy, either at law or in equity. The action at law will lie upon the debt, while, on the other hand, the equitable jurisdiction arises from the power of a Court of Chancery to compel contribution among the shareholders and to effect an equitable distribution among the creditors.¹

In the courts of the United States it is the rule that where a stockholder's statutory liability is by the terms of the statute a joint and several or several liability, the creditor may, after the remedy against the corporation is exhausted, be enforced in an action at law, but in all other cases of statutory liability, the remedy must be in equity, as in cases of unpaid subscriptions.² In several of the State courts it is held that a creditor's remedy against a shareholder upon the statutory liability is in equity

Slate Roofing Co., 16 Minn. 368 (1871); *Culver v. Third National Bank*, 64 Ill. 528 (1871); *Branson v. Oregonian Ry. Co.*, 10 Oregon, 278 (1882).

In Pennsylvania, under the statute relating to the incorporation of manufacturing companies, the corporate creditor proceeds against the shareholders in an action at law upon the original contract, making the corporation and all the shareholders parties defendant. *Brinham v. Wellersburg Coal Co.*, 47 Penn. St. 43 (1864); *Mansfield Iron Works v. Wilcox*, 52 Id. 377 (1866); *Hoard v. Wilcox*, 47 Id. 51 (1864); *McHose v. Wheeler*, 45 Id. 32 (1863). See *Patterson v. Wyomissing Manfg. Co.*, 40 Penn. St. 117 (1861). And compare *Thompson v. Jewell*, 43 Mich. 240 (1880); *Pope v. Leonard*, 115 Mass. 286 (1874); *Branson v. Oregonian Ry. Co.*, 10 Oregon, 278 (1882).

¹ *Bank of the United States v. Dallam*, 4 Dana, 574 (1836); *Van Hook v. Whitlock*, 3 Paige, 409 (1832); *Bank of Poughkeepsie v. Ibbotson*, 24 Wend. 473 (1840); *Masters v. Rossie Lead Mining Co.*, 2 Sandf. Chan. 301 (1845); *Pfohl v. Simpson*, 74 N. Y. 137 (1878); *Eames v. Doris*, 102 Ill. 350 (1882); *Culver v. Third National Bank*, 64 Id. 528 (1871); *Grund v. Tucker*, 5 Kan. 70 (1869); *Perry v. Turner*, 55 Mo. 418 (1874); *Norris v. Johnson*, 34 Md. 485, 489 (1871); *Matthews v. Albert*, 24 Id. 527 (1866). Cf. *Weeks v. Love*, 50 N. Y. 568 (1872); *Story v. Furman*, 25 Id. 214 (1862); *Garrison v. Howe*, 17 Id. 458 (1858). And see the following

New York cases, wherein it seems to be held that where there is a remedy in equity it is exclusive: *Morgan v. New York, &c., R. R. Co.*, 10 Paige, 290 (1843); *Sherwood v. Buffalo, &c., R. R. Co.*, 12 How. Prac. 136 (1855); *Hinds v. Canandaigua, &c., R. R. Co.*, 10 Id. 487 (1855); *Courtois v. Harrison*, 12 Id. 359 (1856). This is not, however, it is believed, the prevailing view in that State.

² Revised Statutes of the United States, § 737; *Ogilvie v. Knox Insurance Co.*, 22 How. 380; *Sawyer v. Hoag*, 17 Wall. 610 (1873); *Pollard v. Bailey*, 20 Id. 520 (1874); *Terry v. Anderson*, 95 U. S. 628, 635 (1877); *Mills v. Scott*, 99 Id. 25 (1878); *Hatch v. Dana*, 101 Id. 205 (1879); *Terry v. Little*, Id. 216 (1879); *Patterson v. Lynde*, 106 Id. 519 (1882). Cf. *County of Morgan v. Allen*, 108 Id. 498 (1880); *Bullard v. Bell*, 1 Mason, 243 (1817); *Wood v. Dummer*, 3 Id. 309; *Marsh v. Burroughs*, 1 Woods, 463; *Holmes v. Sherwood*, 3 McCrary, 405; s. c. 16 Fed. Rep. 725; *Cuykendall v. Miles*, 10 Fed. Rep. 342 (1882). Accordingly in these courts, under a statute making "the persons and property of the stockholders . . . liable for . . . notes . . . in proportion to the number of shares that each individual may hold," the remedy is exclusively in equity. *Mills v. Scott*, 99 U. S. 25 (1878); *Terry v. Tubman*, 92 Id. 156 (1875); *Pollard v. Bailey*, 20 Wall. 520 (1874); *Cuykendall v. Miles*, 10 Fed. Rep. 342 (1882); *Patterson v. Lynde*, 106 U. S. 519 (1882).

alone.¹ In New York, a stockholder sued at law for the enforcement of this liability may institute an equitable proceeding to bring in all the parties.²

§ 227. *Stockholder's defenses against his statutory liability.*—There are two classes of defenses that may occur to a stockholder to defeat his statutory liability. One class is of defenses that the corporation itself might have set up, or did set up, against the plaintiff when he sought to collect his debt from the corporation. As already explained herein, in some jurisdictions, particularly New York, the stockholder may set up these defenses, although the corporation has failed to establish them.* In other and most jurisdictions he cannot.

A second class of defenses include those which are personal to the particular stockholder, and not such as the corporation might have set up. They are largely such defenses as the stockholder might set up against the corporation to defeat his subscription. They do not refer to the validity of the creditor's debt, but they deny that that particular defendant is one of those who are liable for the corporate debts. There are, in addition to the defenses specified in a previous chapter,³ several defenses which are peculiar to this statutory liability.

(a.) *Release.*—A release by the corporate creditor, of one share-

¹ *Smith v. Huckabee*, 53 Ala. 191 (1875); *Perkins v. Sanders*, 56 Miss. 733; *Eames v. Doris*, 102 Ill. 350 (1882). See *Patterson v. Lynde*, 106 U. S. 519 (1882).

² *Garrison v. Howe*, 17 N. Y. 458 (1858). So also in Oregon. *Brundage v. Monumental, &c., Mining Co.*, 12 Oregon, 322 (1885). When the equitable remedy is pursued, the corporation, and all the solvent shareholders within the jurisdiction, who are known, should be made defendants. Contribution among the shareholders is of the essence of this proceeding, and that is best effected when all are made parties. *Walsh v. Memphis, &c., R. Co.*, 2 McCrary, 156 (1881); s. c. 6 Fed. Rep. 797; *Umsted v. Buskirk*, 17 Ohio St. 113 (1866); *Erickson v. Nesmith*, 46 N. H. 371 (1866); *Hadley v. Russell*, 40 N. H. 109; *Brinham v. Wellersburg Coal Co.*, 47 Penn. St. 43 (1864); *Hoard v. Wilcox*, Id. 51 (1864); *Mansfield Iron Works v. Wilcox*, 52 Id. 377 (1866); *McIlrose v. Wheeler*, 45 Id. 32 (1863). The joinder of all the shareholders may be dispensed with in a case where it is shown to be im-

practicable. *Umsted v. Buskirk*, 17 Ohio St. 113 (1866); *Pierce v. Milwaukee Construction Co.*, 38 Wis. 253 (1875); *Coleman v. White*, 14 Wis. 700 (1862); *Crease v. Babcock*, 10 Metc. 525 (1846); *Brundage v. Monumental, &c., Mining Co.*, 12 Oregon, 322 (1885). Two or more creditors may join in an equitable action to enforce the statutory liability of shareholders. *Hickling v. Wilson*, 104 Ill. 54 (1882). And an action to enforce statutory liability may be joined with an action to collect unpaid subscriptions. *Warner v. Callender*, 20 Ohio St. 190 (1870). But a claim against stockholders upon a liability imposed by statute, cannot be joined in one bill in equity with a claim against the directors of the company, although the two claims are derived from the same statute. *Cambridge Water Works v. Somerville Dyeing, &c., Co.*, 14 Gray, 193 (1859); *Pope v. Leonard*, 115 Mass. 286 (1874). Cf. *Wiles v. Suydam*, 64 N. Y. 173 (1876), and see *Douglass v. Ireland*, 73 N. Y. 100 (1878).

³ Chapter X.

holder from his proportion of the corporate indebtedness, will not operate to release the other shareholders.¹ Thus where the shareholders are held to be severally and not jointly liable under the statute, one may be released without releasing the others.²

(b.) *Estoppel*.—Again, the defense of estoppel is sometimes set up. In the English cases it is said that the doctrine of estoppel is a defense to an action to enforce the common law liability on the subscription, but not to an action to enforce a statutory liability.³

(c.) *Liability already paid*.—It is a defense to the stockholder to prove that his full statutory liability has already been paid by him. A stockholder who has voluntarily paid corporate debts to the full extent of his statutory liability, is entitled to set up that fact. And when such a payment was *bona fide* it is a bar to an action to collect any further amount.⁴

¹ *Prince v. Lynch*, 38 Cal. 528 (1869); *Herries v. Platt*, 21 Hun, 132 (1880).

² *Bank of Poughkeepsie v. Ibbotson*, 5 Hill, 561 (1843). *Cf. Herries v. Platt*, 21 Hun, 132 (1880). But whether an extension given to the corporation by a creditor will not discharge a shareholder as to his liability by statute seems uncertain. In the case of *Harger v. McCullough*, 2 Denio, 119 (1846), it was held that it would not, while in the later case of *Parrott v. Colby*, 6 Hun, 55 (1875); s. c. affirmed, 71 N. Y. 597 (1877) (*cf. Aultman's Appeal*, 98 Penn. St. 505 (1881); *Hanson v. Donkersley*, 37 Mich. 184; *Grand Rapids Savings Bank v. Warren*, 52 Id. 557), without expressly overruling *Harger v. McCullough*, it is plainly declared, in making an application of the short Statute of Limitations provided by the General Manufacturing Act of New York (N. Y. Laws of 1848, chap. 40, § 10), that the liability of shareholders in these cases cannot be revived or extended by any renewal or extension of the indebtedness which the creditors may make with the corporation. And in accordance with that view, where the effect of the extension granted by the creditor to the corporation had been to postpone the action against the shareholder beyond the time prescribed by the statute within which such an action is maintainable, that is, one year from the time the corporate debt was first due, it was held that the shareholder was thereby discharged. *Parrott v. Colby*, *supra*. *Acc. Jagger Iron Co. v. Walker*, 76 N. Y. 521 (1879); *Stilphen v. Ware*, 45 Cal. 110. *Cf. Sutherland v. Ol-*

cott, 95 N. Y. 93 (1884); reversing s. c. 29 Hun, 161; *Jones v. Barlow*, 62 N. Y. 202 (1875).

³ *Ness v. Angas*, 3 Exch. 805 (1849); *Ness v. Armstrong*, 4 Id. 21; *Moss v. Steam Gondola Co.*, 17 C. B. 180 (1855); *Bailey v. Universal Provident Life Association*, 1 C. B. (N. S.) 557 (1857). In New York, the admission of one shareholder is inadmissible to charge others with whom he is sued, to enforce their personal liability as stockholders of an insolvent corporation. *Simmons v. Sisson*, 26 N. Y. 264 (1863).

⁴ *Buchanan v. Meisser*, 105 Ill. 638 (1883); *Lane v. Harris*, 16 Ga. 217 (1854); *Belcher v. Willcox*, 40 Id. 391 (1869); *Robinson v. Bank of Darien*, 18 Id. 65, 109 (1855); *Tallmadge v. Fishkill Iron Co.*, 4 Barb. 382 (1848); *Garrison v. Howe*, 17 N. Y. 458 (1858); *Woodruff & Beach Iron Works v. Chittenden*, 4 Bosw. 406 (1859); *Boyd v. Hall*, 56 Ga. 563 (1876); *San Jose Savings Bank v. Pharis*, 58 Cal. 380; *Thompson v. Meisser*, 108 Ill. 359. But when a creditor has actually commenced a suit to enforce the statutory liability of any individual shareholder, it is then too late for that shareholder to defeat the action by paying some other corporate creditor's claim. *Jones v. Wiltberger*, 42 Ga. 575 (1871). Nor will a shareholder, who has employed an agent to buy up claims at a discount, and then confessed judgment in favor of that agent, be permitted to plead such a judgment in bar of an action by other creditors. *Manville v. Karst*, 16 Fed. Rep. 173. Payment of

(d.) *Set-off*.—In a preceding section, it has been shown that, when a shareholder is indebted to the corporation for an unpaid balance of subscription, he cannot set-off, as against that liability, a debt due him from the corporation.¹ He must first pay what he owes to the company, and then come in the same as other creditors, and share ratably in the distribution of the assets. The rule is not so stringent as regards the statutory liability, and the question whether he may set-off a debt owing to him from the corporation, will depend entirely upon the nature of the liability imposed upon him by the statute. If the statute creates a fund, out of which the creditors are to be paid ratably, then the stockholder cannot set-off an indebtedness of the corporation to him. He must pay in what the statute requires, and then prove his claim against the corporation like any other creditor.² But where the shareholder's liability by statute is immediate, and personal, and several, and any creditor may sue any shareholder,

the judgments at a discount is no exhaustion of the liability, though the judgments at full value would have exhausted it. *Kunkelman v. Reutchler*, 15 Brad. (Ill.) 271 (1884). Neither may a shareholder himself buy in claims at a discount, and then set them off at their face value in an action to enforce his statutory liability to creditors. *Gauch v. Harrison*, 12 Bradw. (Ill.) 459; *Thompson v. Meisser*, 108 Ill. 359. *Cf. Diven v. Phelps*, 34 Barb. 224; *Balch v. Wilson*, 25 Minn. 299; *Smith v. Mosby*, 9 Heisk. (Tenn.) 501; *Lonier v. Gayoso Savings Institution*, 9 Id. 506.

¹ See Chapter XI.

² *Smith v. Huckabee*, 53 Ala. 191, 196 (1875); *Buchanan v. Meisser*, 105 Ill. 638 (1883); *Matter of the Empire City Bank*, 18 N. Y. 199, 227 (1858); *Matthews v. Albert*, 24 Md. 527 (1866); *Garrison v. Howe*, 17 N. Y. 458 (1858); *Hillier v. Allegheny Mutual Ins. Co.*, 3 Penn. St. 470; *Lawrence v. Nelson*, 21 N. Y. 158 (1860); *Thebus v. Smiley*, 110 Ill. 316 (1884); *Weber v. Fickey*, 47 Md. 196; *Emmert v. Smith*, 40 Id. 123; *Terry v. Bank of Cape Fear*, 20 Fed. Rep. 777; *Stockton v. Mechanics, &c., Bank*, 32 N. J. Eq. 163, 167; *Grissell's Case*, L. R., 1 Chan. 528; *Black's Case*, L. R., 8 Chan. 254; *Callisher's Case*, L. R., 5 Eq. 214; *Barnett's Case*, L. R., 19 Eq. 449. *Cf. Clapp v. Wright*, 21 Hun, 240 (1860). Where the shareholder's liability is un-

limited, the question of the right to set-off is not material, because each shareholder "is liable to contribute to any amount until all the liabilities of the company are satisfied, and therefore it signifies nothing to the creditors, whether the set-off is allowed or not." *Grissell's Case*, *supra*, p. 536. But see *Briggs v. Penniman*, 8 Cowen, 387 (1826).

Upon this point *Denio, J.*, says: "Under a proceeding for winding up a corporation where an account of all the debts and of the effects, including the aggregate liability of the stockholders, is required to be taken, there is no reason why a creditor should be in any better situation on account of being at the same time a stockholder. In the latter character, the constitution and the statute make him liable to the creditors, to an amount equal to his stock, or to his just proportion of that amount, if the whole is not required, but as a creditor he is entitled only to a dividend in proportion to the other creditors. In case of a deficiency in means to pay all the debts, he must take his dividend *pro rata*. But if he could set-off his claim as a creditor against his liability as a stockholder, he might be paid in full, while the other creditors would receive only a part of the amount due them." *Matter of the Empire City Bank*, 18 N. Y. 199, 227. See *Morawetz on Corporations* (2d edition), § 898; *Taylor on Corporations*, § 731.

then the shareholder may properly set-off a debt owing to him from the corporation, when he is sued by a corporate creditor.¹

(e.) *Interest*.—In South Carolina² and Illinois,³ the shareholder is not liable for interest on the amount for which the statute makes him answerable, and when he pays the principal sum the whole liability is discharged. But in New York, interest is collectible from the time the suit to enforce is commenced.⁴

(f.) *Costs*.—Although it be a condition precedent to the action against the shareholder that a judgment be recovered against the corporation, it is no part of the shareholder's statutory liability to pay the costs of obtaining that judgment. Accordingly a judgment against the shareholder must not include any part of the costs of the proceeding against the corporation.⁵

(g.) *Statute of Limitations*.—Where the liability of the

¹ *Mathez v. Neidig*, 72 N. Y. 100 (1878); *Agate v. Sands*, 73 Id. 620 (1878); *Wheeler v. Millar*, 90 Id. 353, 362 (1882); *Boyd v. Hall*, 56 Ga. 563 (1876); *Remington v. King*, 11 Abb. Prac. 279 (1858). See also *Quick v. Lemon*, 105 Ill. 578. This defense is allowed by the courts of New York in actions to enforce the extraordinary liability imposed by the statute of that State known as the Manufacturing Companies Act of 1848. N. Y. Laws of 1848, chap. 40, §§ 10, 24. See *Wheeler v. Millar*, 90 N. Y. 353 (1882), a case in which the right to set-off under this statute is fully considered. The shareholder's right to set-off his claim against the corporation in defense to an action against him to enforce his statutory liability may sometimes be a matter of *bona fides*. *Boyd v. Hall*, 56 Ga. 563 (1876); *Belcher v. Willcox*, 40 Id. 391 (1869); *Smith v. Huckabee*, 53 Ala. 191 (1875); *Thompson v. Meisser*, 108 Ill. 359.

² *Sacketts Harbor Bank v. Blake*, 3 Rich. Eq. 225 (1849).

³ *Munger v. Jacobson*, 99 Ill. 349 (1881).

⁴ *Handy v. Draper*, 89 N. Y. 334 (1882); *Burr v. Wilcox*, 22 Id. 551 (1860). Cf. *Casey v. Galli*, 94 U. S. 673 (1876). Where a referee computed the interest on the plaintiff's claim from the date on which it became due from the company, instead of from the day the suit against the shareholder was commenced, it appearing that the indebtedness was less than the amount of the

shareholder's liability, and that the allowance of interest did not swell it beyond that limit, the Court of Appeals held such a computation no error. *Wheeler v. Millar*, 90 N. Y. 353, 362 (1882), and apparently upon sufficient ground, the court, by Finch, J., saying: "The creditor's debt consists both of principal and interest. He is just as much entitled to the latter as the former, and the liability to pay the debt must necessarily include the accrued interest up to the statutory limit. When that is reached any further interest runs only upon that sum from the date of the commencement of the action. The entire principal and interest of the debt in the present case did not exceed the limit of liability, and the allowance of interest from the maturity of the debt was, therefore, proper and violated no right of the defendant." *Wheeler v. Millar*, *supra*, p. 363. Cf. *Corning v. McCullough*, 1 N. Y. 47, 54 (1847); *Cole v. Butler*, 43 Me. 401 (1857). So in Michigan, the shareholder is liable for interest. *Grand Rapids Savings Bank v. Warren*, 52 Mich. 557 (1884); *Cleveland v. Burnham*, 64 Wis. 347 (1885).

⁵ *Bailey v. Bancker*, 3 Hill, 188 (1842); *Rorke v. Thomas*, 56 N. Y. 559, 565 (1874). Cf. *Miller v. White*, 50 N. Y. 137 (1872). It is possible that the rule might be otherwise in a case where the judgment is held to be conclusive as against the shareholder. So in Michigan, *Grand Rapids Savings Bank v. Warren*, 52 Mich. 557 (1884).

shareholder is immediate and primary, and not contingent on the obtaining of a judgment against the corporation, it is clear that the Statute of Limitations begins to run in favor of the shareholder when the debt matures against the corporation.¹

But when the creditor must first obtain a judgment against the corporation and sue out an execution, which must be duly returned wholly or partially unsatisfied before the cause of action arises against the shareholder on his statutory liability, then the Statute of Limitations commence to run upon the return of the execution.²

It is a general rule of law that the Statute of Limitations obtaining in any jurisdiction, and applicable to an ordinary action to enforce a contract, is the one applicable to the action to enforce the statutory liability of shareholders in incorporated companies.³

Accordingly the suit must usually be commenced within six years after the cause of action has accrued.⁴

¹ *Davidson v. Rankin*, 34 Cal. 503 (1868); *Lindsay v. Hyatt*, 4 Edw. Chan. (N. Y.) 97. Compare *Carrol v. Green*, 92 U. S. 509 (1875); *Terry v. Tubman*, 92 Id. 156 (1875); *Terry v. McLure*, 103 Id. 442 (1880); *Corning v. McCullough*, 1 N. Y. 47 (1847). See also *Allibone v. Hager*, 46 Tenn. St. 48; *Terry v. Calnan*, 13 S. C. 220; *Lawler v. Burt*, 7 Ohio St. 340; *King v. Duncan*, 38 Hun, 461 (1886).

² *Handy v. Draper*, 89 N. Y. 334 (1882); *Merritt v. Reid*, 13 Week. Dig. (N. Y.) 453; *Longley v. Little*, 26 Me. 162. In *Terry v. Tubman*, 92 U. S. 156 (1875), where the charter of a bank contained a provision making the shareholders individually liable for the ultimate redemption of its bills, the liability of the shareholders was held to arise, and hence the Statute of Limitations to commence to run in their favor, upon the open and notorious insolvency of the bank. So likewise where shareholders were made individually liable "upon the failure of the bank" it was held that the liability arising upon the failure, the Statute of Limitations began to run at that time. *Carrol v. Green*, 92 U. S. 509, 511 (1875). To the same effect, is *Baker v. Atlas Bank*, 9 Mete. 182 (1845); *Terry v. McLure* 103 U. S. 442, (1880); *Godfrey v. Terry*, 97 Id. 171, (1877).

³ *Green v. Beckman*, 59 Cal. 545

(1881); *Corning v. McCullough*, 1 N. Y. 47 (1847); *Wiles v. Suydam*, 64 Id. 173, 176 (1876); *Mappier v. Mortimer*, 11 Abb. Prac. (N. S.) 455; *Salt Lake City National Bank v. Hendrickson*, 40 N. J. Law, 52; *Baker v. The Atlas Bank*, 9 Mete. 182 (1845); *The Commonwealth v. The Cochituate Bank*, 3 Allen, 42; *Norris v. Wrenschall*, 34 Md. 492; N. Y. Code of Civil Procedure, § 382. Compare *Merchants' Bank of New Haven v. Bliss*, 21 How. Prac. 366; s. c. 13 Abb. Prac. 234; 1 *Robertson* (N. Y. Super. Ct.), 401; 35 N. Y. 414 (1866).

⁴ The citations in the preceding note. See also *Phillips v. Therasson*, 11 Hun, 141 (1877); *King v. Duncan*, 38 Id. 461 (1886); *Knox v. Baldwin*, 80 N. Y. 610 (1880); *Hawkins v. Furnace Co.*, 40 Ohio St. 507 (1884). In South Carolina, under the Statute of Limitations of 1712 in that State, this action must be begun within four years. *Carrol v. Green*, 92 U. S. 509 (1875); *Terry v. McLure*, 103 Id. 442 (1880); and, on the other extreme, in some of the older cases, it is held that an obligation, such as this, to pay money, arising under a statute, is a debt by specialty, and accordingly that it is barred only by a lapse of twenty years. *Bullard v. Bell*, 1 Mason, 243, 289, (1817 by Judge Story); *Thornton v. Lane*, 11 Ga. 459 (1852); *Lane v. Morris*, 10 Id. 162 (1851). But see this view condemned

If a statutory liability be held to be a penalty, then of course, it will be held to come within that provision of the Statute of Limitations which provide for action to enforce penalties.¹

In general, whatever the statute be, it is the rule that a lapse of time sufficient to constitute a bar at law, will in equity be given the same effect ; which is to say that in these cases there is the same Statute of Limitations both at law and in equity.²

§ 228. *Priority among creditors*.—When the creditor is entitled to an action at law against an individual shareholder for an enforcement of a statutory liability, in order to collect a claim against the corporation, it is a general rule that the creditor first suing any shareholder is entitled to priority in enforcing his claim as against that particular shareholder. The diligent creditor is entitled to the payment of his claim, although other creditors are thereby deprived of payment.³ The right to a priority, however, in these cases, is in general one of questionable propriety, and the courts are not inclined to favor it.⁴ And one creditor

in *Carrol v. Green*, 92 U. S. 509, 515 (1875), in an opinion by Justice Swayne, construing the South Carolina statute of 1712. *Cf. Green v. Beckman*, 59 Cal. 545 (1881), construing § 359 California Code of Civil Procedure.

¹ *Gridley v. Barnes*, 103 Ill. 211; *Diversey v. Smith*, Id. 378. See also *Cable v. McCune*, 26 Mo. 380; *Lawlor v. Burt*, 7 Ohio St. 340; *Cody v. Smith*, 12 Neb. 628; *Knox v. Baldwin*, 80 N. Y. 610, (1880). *Cf. Duckworth v. Roach*, 81 N. Y. 49 (1880).

² *Bank of Poughkeepsie v. Ibbotson*, 24 Wend. 473 (1840); *Carrol v. Green*, 92 U. S. 509 (1875); *Baker v. The Atlas Bank*, 9 Metc. 182 (1845); *Lindsay v. Hyatt*; 4 Edw. Chan. (N. Y.) 104. When the statute prescribes the limitation there is of course no controversy. *Baker v. Bachus' Admr.*, 32 Ill. 99. In the New York Manufacturing Companies Act (N. Y. Laws of 1848, chap. 40) it is provided (§ 24) that "No stockholder shall be personally liable for the payment of any debt contracted by any company formed under this act, which is not to be paid within one year from the time the debt is contracted, nor unless a suit for the collection of such debt shall be brought against such company within one year after the debt shall become due, and no suit shall be brought

against any stockholder who shall cease to be a stockholder in any such company, for any debt so contracted, unless the same shall be commenced within two years from the time he shall have ceased to be a stockholder in such company." Provisions in substance the same as this may be found in the general statutes of most of the States.

³ *Cole v. Butler*, 43 Me. 401 (1857); *Ingalls v. Cole*, 47 Id. 530, 541 (1860); *Jones v. Wiltberger*, 42 Ga. 575 (1871); *Robinson v. Bank of Darien*, 18 Id. 65, 108 (1855); *Thebus v. Smiley*, 110 Ill. 316; *Jones v. Arkansas, &c., Co.*, 38 Ark. 17. See also *Weeks v. Love*, 50 N. Y. 568 (1872); *Miers v. Zanesville, &c., Turnpike Co.*, 13 Ohio, 197. Accordingly, after the creditor commences his action, the shareholder cannot defeat him by paying voluntarily some other creditor, and thereby exhausting his liability. *Jones v. Wiltberger, supra*; *Thebus v. Smiley*, 110 Ill. 316 (1884), holding also that a stockholder sued by a single creditor may bring a suit in equity to bring in all the stockholders and creditors.

⁴ *State Savings Association v. Kellogg*, 6 Mo. App. 540; *Wright v. McCormack*, 17 Ohio St. 86; *Smith v. Huckabee*, 53 Ala. 191; *Chicago v. Hall*, 103 Ill. 342. *Cf. Ballston Spa Bank v. Marine*

may, at the instance of the rest, be restrained from the prosecution of his individual suit where it is in prejudice of the equal rights of all the others.¹ In general incorporated companies are not allowed in case of insolvency to make assignments with preferences.²

When the proceeding to enforce the statutory liability is in equity there can be, upon plain principles, no priority among creditors. The fund from which corporate debts are paid belongs equally in equity to all the creditors, and cannot be appropriated by either debtor or creditor to the payment of one claim to the prejudice or exclusion of others.³

§ 229. *Contribution among shareholders.*—Upon general principles of equity, where a shareholder has been held liable, under the provisions of a statute, for a debt of the corporation of which

Bank, 18 Wis. 490 (1864); *Pierce v. Milwaukee Construction Co.*, 38 Id. 253 (1875); *Courtois v. Harrison*, 12 How. Prac. 359; *Lowber v. Mayor*, 5 Abb. Prac. 268 (1857); *McBride v. Farmers Bank*, 28 Barb. 476 (1858); *Rankine v. Elliott*, 16 N. Y. 377 (1857); *State v. Bank of Maryland*, 6 Gill & J. 205; *Shockley v. Fisher*, 75 Mo. 498; *Lionberger v. Broadway Savings Bank*, 10 Mo. App. 499, and particularly *Savings Bank v. Bates*, 8 Conn. 505; *Whitwell v. Warner*, 20 Vt. 425; *Ringo v. Briscoe*, 13 Ark. 563; *Arthur v. Commercial, &c., Bank*, 17 Miss. 394. *Cf.* *Catlin v. Eagle Bank*, 6 Conn. 233; *Hopkins v. Gallatin Turnpike Co.*, 4 Humph. (Tenn.) 403; *Union Bank v. Ellicott*, 6 Gill & J. 363; *Pope v. Brandon*, 2 Stewart (Ala.), 401. The national banks are forbidden by statute from making assignments with preferences. U. S. Rev. Stat. § 5242. See *Irons v. Manufacturers National Bank*, 6 Biss. 301, and in New York a statute prevents assignments by incorporated companies *in toto*, the intent of the statute apparently being to prevent preferences in any shape. 1 R. S. chap. 18, title 4, § 4 (7th edition, p. 1534).

¹ *Eames v. Doris*, 102 Ill. 350 (1882); *Marr v. Bank of West Tennessee*, 4 Cald. 471, 483-486; *Pfohl v. Simpson*, 74 N. Y. 137 (1878). *Cf.* *Garrison v. Howe*, 17 N. Y. 458 (1858).

² *Robins v. Embry*, 1 Sm. & M. Chan.

(Miss.) 207, 258; *Bodley v. Goodrich*, 7 How. 276; *Swepson v. The Bank*, 9 Lea (Tenn.), 713; *Richards v. New Hampshire Ins. Co.*, 43 N. H. 263. But see for an apparently contrary view, *Ardesco Oil Co. v. North American Oil, &c., Co.*, 66 Penn. St. 375. See also *Ladd v. Cartwright*, 7 Oregon, 329; *Patterson v. Lynde*, 106 U. S. 519 (1882). A shareholder, it is said, being also a creditor of the corporation, may make use of whatever advantage his position as shareholder gives him to secure the payment of his claim, even to the exclusion of other creditors who are not shareholders. *Whitwell v. Warner*, 20 Vt. 425, 444; *Reichwald v. Commercial Hotel Co.*, 106 Ill. 439. See also *Bristol Milling, &c., Co. v. Probasco*, 64 Ind. 406; *Terry v. Bank of Cape Fear*, 20 Fed. Rep. 777; *Osgood v. Ogden*, 4 Keyes (N. Y.), 70.

³ *Sawyer v. Hoag*, 17 Wall. 610; *Scoville v. Thayer*, 105 U. S. 143, 152; *Bisbit v. Kentucky River Navigation Co.*, 15 Fed. Rep. 353 (and the note); *Cochran v. Ocean Dry Dock Co.*, 30 La. Ann. 1865; *Williams v. Traphagen*, 38 N. J. Eq. 57; *Goodwin v. McGehee*, 15 Ala. 216; *Lexington, &c., Insurance Co. v. Page*, 17 B. Mon. 412; *Life Association v. Levy*, 33 La. Ann. 1203; *Terry v. Bank of Cape Fear*, 20 Fed. Rep. 777; *Long v. Pennsylvania Insurance Co.*, 6 Penn. St. 421, and the cases generally cited in the preceding notes.

he is a member, he may maintain an action against his co-shareholders for contribution.¹

¹ *Aspinwall v. Sacchi*, 57 N. Y. 331 (1874); *Stewart v. Lay*, 45 Iowa, 604 (1877); *Umsted v. Buskirk*, 17 Ohio St. 113; *Matthews v. Albert*, 24 Md. 527; *Hadley v. Russell*, 40 N. H. 109, 112; *Erickson v. Nesmith*, 46 Id. 371; *Gray v. Coffin*, 9 Cush. 192; *Middletown Bank v. Magill*, 5 Conn. 61; *Brinham v. Wellersburg Coal Co.*, 47 Penn. St. 43; *Masters v. Rossie Lead Mining Co.*, 2 Sandf. Chan. 301; *Farrow v. Bivings*, 13 Rich. Eq. 25, and the cases generally, *supra*. See *Spackman v. Evans*, L. R. 3 House of Lords, 171, 197. *Of. Ray v. Powers*, 134 Mass. 22; *O'Reilly v. Bard*, 105 Penn. St. 569; *Hartman v. Ins. Co. of Valley of Va.*, 32 Gratt. 242; *Chandler v. Brown*, 77 Ill. 334; *Bronson v. Wilmington, &c., Insurance Co.*, 85 N. C. 411; *Morawetz on Corp.* (2d edition), §§ 311-315; *Lindley on Partnership*, pp. 1223-1474.

CHAPTER XIII.

LIABILITY AS PARTNERS AND FOR ASSESSMENTS BEYOND THE PAR VALUE OF THE STOCK.

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| § 230. Different liabilities of a stockholder. | § 237-39. Liability as partners by reason of migration of corporation. |
| 231-33. Liability as partners by reason of deficient incorporation. | 240. Liability as partners by reason of abandoned enterprise. |
| 234. Instances. | 241-42. Assessments in excess of par value of stock. |
| 235. Extent of the liability. | 243. Miscellaneous cases of liability. |
| 236. Liability as partners by reason of unauthorized incorporation. | |

§ 230. *Different liabilities of a stockholder on his stock.*—A stockholder may be said to be liable on his stock in three different ways. He is liable to the corporation and corporate creditors until the full par value of his stock has been paid.¹ Second, he may have an additional liability imposed upon him by statute.² Third, it may happen that by some accident, mistake, or neglect the supposed corporation was never duly incorporated, thereby leaving the members liable as partners in a copartnership; or such a liability may arise in other ways; or it may be within the power of the corporation to assess the stockholder for sums over and above and in addition to the par value of the stock. This third kind of liability is unusual in its character, and is the subject of this chapter.

§ 231. *Liability as partners by reason of material defects in becoming incorporated.*—The statutes under which incorporations are generally made provide that a corporation may be formed by taking certain steps, usually the making and filing with the State, and also with the local authorities, a certificate signed by the incorporators, and containing a statement of the business, of the capital stock, and other facts material to the organization of the corporation.

Occasionally, however, it happens that this certificate is not fully made out, as required by the statute, or is not filed, or some

¹ See Chapters XI and VII.

² See Chapter XII.

other step prescribed by law is not complied with. The corporation is then not duly incorporated, and the State, by *quo warranto*, may oust it from its user of corporate franchises. But it is a difficult question to determine whether a private individual may take advantage of such facts and claim that the supposed corporation is not a corporation, but only a partnership.

§ 232. *When the regularity of acts in becoming incorporated cannot be questioned by a private individual.*—As already explained,¹ a subscriber for stock in a corporation cannot, when sued for calls on his stock, set up that the corporation was not duly incorporated. He is estopped from so doing. Nor can a stockholder, who has funds of the corporation in his hands, defeat an action by the corporation therefor by setting up that the corporation was not duly incorporated.² And in general, a party contracting to pay money to a corporation, or to transfer property to it as a corporation, cannot avoid the obligation of that contract by alleging the fact that the corporation was not duly incorporated, provided that such corporations were allowed by law.³ Nor, on the other hand, can the corporation itself avoid its contracts on such grounds.⁴

§ 233. *When the regularity of the incorporation may be questioned by a private individual.*—A corporate creditor seeking to enforce the payment of his debt may, however, ignore the existence of the corporation, and may proceed against the supposed stockholders as partners, by proving that the prescribed method of becoming incorporated was not complied with by the company in question.⁵ He is not estopped from so doing, since

¹ See Chapter X; *Buffalo & A. R. R. Co. v. Cary*, 26 N. Y. 75.

² *Krutz v. Paola Town Co.*, 20 Kan. 397 (1878).

³ See 19 Am. Dec. 67, notes; *Lessee of Frost v. Frostbury Coal Co.*, 24 How. 278 (1860), where the grantor of land to a corporation claimed that no title passed. *Pope v. Capital Bk.*, 20 Kan. 440 (1878), where the plaintiff corporation sued the defendant on a promissory note. *Fay v. Noble*, 7 Cush. 188, where a third person was not allowed to impeach a transfer of property by a corporation by setting up that the transfer was invalid owing to informalities in the incorporation.

⁴ *Holbrook v. St. Paul Fire & M. Ins. Co.*, 25 Minn. 229 (1878).

⁵ It is submitted that the clear weight of authority, as shown by a close study of the cases, supports this rule. And it is difficult to see how a contrary rule can be justified or applied. There are several grades of associations, from the ordinary partnership up to the full corporation. First, the unincorporated joint-stock company, where clearly all expect to be liable, and are liable as partners. (See Chapter on Joint stock Companies.) Then the unincorporated joint-stock company, where the members think they are not liable, and contracts are made under that impression. They are still liable as partners. Then might be mentioned an association where the members directed an incorporation to be had, but none is had.

he is not repudiating a contract, but is enforcing it. The fact that he contracted with them under a corporate name is immaterial, since, at common law, parties may carry on business under any name they choose.

§ 234. *Instances.*—Thus it has been held, where the articles of association are signed, but not filed until some time subsequently, that debts contracted in the *interim* may be collected from the stockholders as partners.¹ So also a total failure to file or record the certificate or articles of incorporation renders the members liable as partners;² as does an omission of the members to sign and publish the articles of association;³ or an indefinite

Clearly here, too, they are liable as partners. Again, where the incorporation is but partially completed, there is no reason why the members should be exempt from liability as partners. And such is the effect of the rule given above. In all these cases the *bona fides* of the members, or the understanding of the person with whom they contract, or the fact that the contract is made in the name of a corporation or company, is immaterial. Any partnership or single individual may transact business under the name of a company. (See *Lauferty v. Wheeler*, 11 Abb. N. C. 223.) The law holds that in all the above mentioned cases the members are liable as partners. The author cannot agree with Morawetz in his learned work on Corporations (2d ed., § 748), where a contrary view is taken. The case of *Chaffe v. Ludeling*, 27 La. Ann. 607 (1875), well says: "Obligors are bound not by the style which they give to themselves, but by the consequences which they incur by reason of their acts. It matters not what they choose to call themselves." See also *Natl. Bk., &c. v. Landon*, 45 N. Y. 410 (1871); *Ridenour v. Mayo*, 40 O. St. 9 (1883); and cases *infra*.

¹ *Bigelow v. Gregory*, 73 Ill. 197 (1874). See also *Bergen v. Porpoise F. Co.*, 13 Am. & Eng. Corp. Cas. 1 (N. J., 1886).

² *Field v. Cooks*, 16 La. Ann. 153 (1861); *Abbott v. Omaha Smelting Co.*, 4 Neb. 416 (1876); *Garnett v. Richardson*, 35 Ark. 144 (1879); *Ferris v. Thaw*, 72 Mo. 449 (1880); *First Natl. Bank of Davenport v. Davies*, 43 Iowa, 424 (1876); *Coleman v. Coleman*, 78 Ind. 344 (1881); *Martin v. Fewell*, 79 Mo. 401, 410 (1883). In the case of *Hurt v. Salisbury*, 55 Mo.

310 (1874), corporate officers were held personally liable on a promissory note signed by them as officers, where the certificate of incorporation was not filed as required. In *Richardson v. Pitts*, 71 Mo. 428 (1879), the same officers were held to be entitled to contribution from other members of the supposed corporation. In the case *De Witt v. Hastings*, 69 N. Y. 518 (1877), where no certificate was filed, owing to an abandonment of the enterprise, it was held that a subsequent filing of it could not render liable one of the original promoters who took no part in the filing of the articles of association, although his name was attached thereto. *Cf. Blanchard v. Kaul*, 44 Cal. 440 (1872). *Contra*, *Planters, &c., Bk. v. Padgett*, 69 Ga. 159 (1882); *Humphreys v. Mooney*, 5 Colorado, 282 (1880); *Gartside Coal Co. v. Maxwell*, 22 Fed. Rep. 197 (1884); *Merriman v. Magivennis*, 12 Heisk. (Tenn.) 494 (1873); *Merchants, &c., Bk. v. Stone*, 38 Mich. 779 (1878). *Cf. Harrod v. Hamer*, 32 Wis. 162 (1873), where the statute effected an incorporation without a filing, but prohibited organization until after the articles were filed. So also where the certificate or articles are to be filed both with the State and the local authorities, a failure as to the former does not render the stockholders liable as partners, provided the articles or certificate are filed with the local authorities. *Makelumne Hill Min. Co. v. Woodbury*, 14 Cal. 424 (1859); *Cross v. Pinckneyville Mill Co.*, 17 Ill. 54. The creditor cannot sue the directors for damages for a fraudulent conspiracy herein, especially when he was informed that the corporation had been irregularly incorporated. *Nelson v. Luling*, 62 N. Y. 645 (1875).

³ *Unity Ins. Co. v. Cram*, 43 N. H.

statement of where the principal place of business of the corporation is to be.¹ The mere assumption of corporate powers, without any attempt at incorporation, cannot, of course, protect the members from full liability.² It is not, however, every omission to comply with the statute that renders the members liable as partners. Immaterial provisions, or requisites to be complied with after incorporation, have not that effect.³ Thus, a failure to commence the principal business⁴ does not invalidate the incorporation, nor does an *ultra vires* act or fraud of the corporation have that effect.⁵

§ 235. *Extent of the liability by reason of deficient incorporation.*—The mere fact that an attempted incorporation has failed does not necessarily render all the participants therein liable absolutely for the debts of the concern. At the most, each is liable only in case he would be liable if the original plan had been to form a partnership. If he was not a member when the debt was contracted he cannot be held liable on that particular debt.⁶ One case goes still farther, and holds that one who becomes a member, subsequently to the attempted incorporation, but takes no part in the organization or management of the company, cannot be held liable for its debts.⁷

§ 236. *Liability as partners by reason of fact that corporations cannot be organized for the business involved.*—The general incorporating acts, common to most of the States, usually specify the particular kinds of business for the prosecution of

636 (1862); *Kaiser v. Lawrence S. Bk.*, 56 Iowa, 104 (1881), where the articles were not properly signed and acknowledged. This case also disapproves the decision in *Humphrey v. Mooney*, 1 Colorado, 193. In enforcing this partnership liability, the assumed corporation is not to be made a party defendant with the members thereof. *Smith v. Colorado Fire Ins. Co.*, 14 Fed. Rep. 399 (1882).

¹ *Harris v. McGregor*, 29 Cal. 124 (1865).

² *Pettis v. Atkins*, 60 Ill. 454 (1871); *Fuller v. Rowe*, 57 N. Y. 23 (1874).

³ Thus a failure to notify each member of the meeting to organize is immaterial. *McClinch v. Sturgis*, 72 Me. 288 (1881).

⁴ *Trowbridge v. Scudder*, 66 Mass. 83 (1853).

⁵ *Langan v. Iowa & Minn. Con. Co.*, 49 Iowa, 317 (1878); *Second Natl. Bk. of*

Cin. v. Hall, 35 O. St. 158 (1878). Where, however, an incorporated society used all its funds to contest a debt, the court compelled the members to replace the money so used. *Admr. of Bigelow v. Cong. Society of M.*, 11 Vt. 283 (1839). In the case *Medill v. Collier*, 16 O. St. 599, 613 (1866), the court says: "When the entire business carried on by persons in the name of a corporation is such as the corporation is prohibited by law from doing, they cannot interpose the corporate privileges between them and the liabilities which the law imposes upon individuals in the transaction of similar business without the use of the corporate name."

⁶ *Fuller v. Rowe*, 57 N. Y. 23 (1874).

⁷ *Stafford Bk. v. Palmer*, 47 Conn. 443 (1880). *Cf. Richardson v. Pitts*, 71 Mo. 128 (1879).

which corporations may be formed thereunder. It follows, that no business can be carried on by persons, as a corporation, under the incorporating act, unless that particular business is specified therein.¹ Frequently certain kinds of business are not mentioned in the act, for the reason that it is not deemed wise public policy to allow a limited liability in that class of business. This seems to have been the rule as regards construction companies for the building of railroads,² and as regards a general mercantile business. Accordingly where the business for which incorporation is sought is not within the classes of business mentioned in the act itself, the attempted incorporation is void, and the participants are liable as copartners.

§ 237. *Liability as partners by reason of migration of corporation.*—By the comity of States the rule has become well established that a corporation organized under the laws of a State may transact business beyond the borders of that State.³ But in

¹ Thus, where a rifle club attempted incorporation under the statute allowing incorporation for "literary, scientific, and charitable purposes," the members are individually liable for damages to the widow of a man who was killed by a bear which the club was keeping. *Vredenburg v. Behan*, 33 La. Ann. 627 (1881). See also *Glen v. Breard*, 35 La. Ann. 875 (1883). There may be a question as to the validity of the law itself allowing the incorporation. *Williams v. Bk. of Michigan*, 7 Wend. 540 (1831); *State of Michigan v. Howard*, 1 Mich. 512 (1846); *Chenango Bridge Co. v. Paige*, 83 N. Y. 178, 190 (1880).

² The New York Business Companies Act of 1875 (ch. 611), expressly excludes railroad construction companies from incorporation under that act. In the following statutes authorizing the incorporation of railroad corporations, the words used do not authorize corporations to "construct," but read "for the purpose of constructing, maintaining, and operating railroads." N. Y. Sess. L. 1850, ch. 140, § 1; Laws of Michigan, § 3313; *Brightley's Purdon's Digest* (Penn.) 1414; Stat. of Ill., ch. 114, § 1; Ind. R. S., ch. 37 (1885). In Ohio, on the other hand, there may be an incorporation "for any purpose for which individuals may lawfully associate themselves, except for dealing in real estate, or carrying on professional business." R. S.

(1886), § 3235. But railroad construction companies must file a statement of the termini, &c., of the railroad itself. § 3237.

It has been held, however, that under the general act for the incorporation of companies for constructing and operating a railroad, a company for the construction alone of the road may be incorporated. "That there can be a railroad company which does nothing but construct the road, and a railroad company which does nothing but operate the constructed road, cannot be doubted. It is not essential to the idea of a railroad company that it should both construct and operate a railway." *First Natl. Bk. of Davenport v. Davies*, 43 Iowa, 424 (1876); *Langan v. Iowa & Minn. Construction Co.*, 49 Iowa, 317 (1878).

³ "It is very true that a corporation can have no legal existence out of the boundaries of the sovereignty by which it is created. . . . But although it must live and have its being in that State only, yet it does not by any means follow that its existence there will not be recognized in other places; and its residence in one State creates no insuperable objection to its power of contracting in another." *Ch. J. Marshall, in Bank of Augusta v. Earle*, 13 Pet. 521. See also *Angell & Ames on Corp.*, § 278; *Taylor on Corp.*, Ch. VII, Part V; *Wood's Field on Corp.*, § 225; *Potter on*

order that such contracts should be upheld, and the corporate character be sustained, it is necessary that both the State creating the corporation, and also the corporation so created, shall have acted in good faith in conferring and taking the corporate privileges. Thus, where a corporation was incorporated by the legislature of Pennsylvania, and authorized to do business anywhere but in that State, the court of Kansas refused to recognize its corporate character.¹ The comity of States does not prevail to that extent.

§ 238. A corporation must have obtained its franchises in good faith, in order to preserve its corporate character in its contracts, and shield its members from personal liability on such contracts. In New Jersey, at an early day, it was held that a corporation could not become incorporated under the laws of New York for the purpose of carrying on all its corporate transactions in the State of New Jersey.² The stockholders were declared to be merely partners. Likewise it was held that where a corporation was incorporated to do business in a certain city in the State, but actually does all its business in another city of that State, the incorporation is a fraud upon the law, and the company is the same as though unincorporated.³ This doctrine was followed in a New York case, in an inferior court, the facts being that a New Jersey corporation had no office or place of business in New Jersey, and did no business there, but transacted its business in New York.⁴

Corp., § 10; Morawetz on Corp., §§ 359-361 (2d ed.).

¹ *Land Grant Ry. & Trust Co. v. Coffey County*, 6 Kans. 245, the court saying: "No rule of comity will allow one State to spawn corporations, and send them forth into other States to be nurtured, and do business there, when said first mentioned State will not allow them to do business within its own boundaries."

² The corporation "cannot be recognized by any court in New Jersey as a legally constituted corporation, nor be dealt with as such. If it can be, what need is there of any general or special law in our State. Individuals, desirous of carrying on any manufacturing business, may go into the city of New York, organize under the general laws of that State, erect all their manufacturing estab-

lishments here, and under their assumed name, transact their business, not only free from all personal responsibility, but under cover of a corporation not amenable to our laws." *Hill v. Beach*, 12 N. J. Eq. R. 31 (1858).

³ The corporation was incorporated to do business in Trenton, but actually transacted all its business in Jersey City. The court said: "The doctrine that the organization cannot be inquired into collaterally, has no application as the case stands, because the charter does not fit this company, and was not intended for it." *Booth v. Wonderly*, 36 N. J. L. 250 (1873).

⁴ "It was not an existing corporation within the meaning of the statute of New Jersey, under which it purports to have been incorporated. . . . It was a fraud upon the laws of New Jersey, and

§ 239. A much more broad and liberal view of the comity of States and the interests of business was taken by the New York Court of Appeals in the case of *Merrick v. Van Santvoord*, where, although a Connecticut corporation did all its corporate business and performed all its corporate acts in New York, excepting the holding of elections, yet the court, in a well considered and ably written opinion, held that the corporation did not thereby lose its corporate character, and that its members were not liable as co-partners.¹ This view of the law has been taken also by the Supreme Court of the State of Ohio.²

§ 240. *Liability for corporate debts where the enterprise is abandoned before incorporation.*—The questions sometimes arise whether a subscriber for stock in a projected corporation is liable to its creditors, in case the enterprise is abandoned before incorporation; and also whether the promoters of the abortive corporation are liable to the subscribers for deposits made by the latter. The former question is decided in the negative. "The subscribers to the stock or articles of association are not partners with those who assume the risk of acting for a corporation not yet legally established."³ As to the latter question, the rule has be-

cannot screen defendants and its organizers from personal responsibility as partners for contracts made in New York under the assumed name." *Kruse v. Dusenbury*, 19 Weekly Dig. (N. Y. Com. Pl.) 201 (1884).

¹ *Merrick v. Van Santvoord*, 34 N. Y. 207 (1866), the court saying: "We think the recognition, in our State, of the rights hitherto conceded in our courts to foreign corporations, is neither injurious to our interests, repugnant to our policy, nor opposed to the spirit of our legislation. . . . It would be neither provident nor just to inaugurate a rule which would unsettle the security of corporate property and rights, and exclude others from the enjoyment here of privileges which have always been accorded to us abroad. . . . A corporation is an artificial being, and has no dwelling, either in its office, its warehouses, its depots, or its ships. . . . The grant of franchises without restriction is equivalent to a specific authority to exercise them wherever the company might find it convenient or profitable, whether with- in or without the limits of the State of

Connecticut." See also *Danforth v. Penny*, 3 Mete. 564.

² Second Natl. Bk. of Cin. v. Hall, 35 Ohio St. 158 (1878), the court holding it to be no fraud on the Ohio laws for a corporation organized under the laws of Kentucky to do all its business in Ohio, even though thereby the stockholders escaped a personal liability.

³ *Ward v. Brigham*, 117 Mass. 24 (1879), the court saying also: "Those who acted as agents for the inchoate corporation acted without a principal behind them, because there was no body corporate capable of appointing agents, and so became principals in the transaction." See also *Duke v. Andrews*, 2 Ex. 290; *Hutton v. Thompson*, 3 H. L. Cas. 161; *Duke v. Diver*, 1 Ex. 36, where the stockholder had promised to pay on a certain day, and was held to his promise. To same effect, *Duke v. Forbes*, Id. 356; *Aldham v. Brown*, 7 E. & B. 164; 2 E. & E. 398, on appeal; *Woolmer v. Toby*, 10 Q. B. 691. However, in the case of *Lake v. Duke of Argyll*, 6 Q. B. 477 (1844), the court held that attendance at a meeting, announcement of intention of being pres-

come well established in England that a subscriber for stock in a corporation that never comes into existence, who has paid a part of his subscription, may recover back from the promoters of the enterprise the amount so paid, and is not liable even for the preliminary expenses.¹ His remedy may be by bill in equity.² If, however, the subscriber expressly or by implication authorizes expenditures, he cannot recover back his deposit.³

§ 241. *Assessments by the corporation in excess of the par value of the stock.*—It is a principle of law, coeval with the existence of corporations having a capital stock, that unless the corporate charter or a constitutional statute provides otherwise, a stockholder, the full par value of whose stock has been paid in, is not liable and cannot be made to pay any sums in addition thereto.⁴ The mere legislative act of creating a corporation cre-

ident and of taking stock, and concurrence in measures for incorporation, may be strong evidence that defendant "held himself out as a paymaster to all who executed the orders." The question, then, is for the jury.

¹ *Ashpittel v. Sercombe*, 5 Ex. 147 (1850), where the court says: "There seems to be no doubt that the plaintiff, having paid his money for shares in a concern which never came into existence, or a scheme which was abandoned before it was carried into execution, has paid it on a consideration which has failed, and may recover it back as money had and received to its use, unless he can be shown to have consented to or acquiesced in the application of the money which the directors have made." See also *Thompson on Liabilities of Officers, &c.*, 210; *Nockels v. Crosby*, 3 B. & C. 814, the leading case; 1 *Lindley on Partnership* (4th ed.), 119, citing *Walstab v. Spottiswoode*, 15 M. & W. 501; *Moore v. Garwood*, 4 Ex. 681; *Coupland v. Challis*, 2 Ex. 682; *Owen v. Challis*, 6 C. B. 115; *Ward v. Londesborough*, 12 C. B. 52; *Mowatt v. Londesborough*, 3 E. & B. 307, and 4 Id. 1. See also *Vallans v. Fletcher*, 1 Ex. 20; *Chaplin v. Clarke*, 4 Ex. 402.

² 2 *Lindley on Partnership* (4th ed.), 954, citing *Harvey v. Collett*, 15 Sim. 332, before the Judicature Acts; and *Cooper v. Webb*, 15 Sim. 454; *Wilson v. Starhope*, 2 Call. 629; *Afferby v. Page*, 1 Ph. 779; *Clements v. Bowers*, 17 Sim. 167; *Sheppard v. Oxenford*, 1 K. & J.

491; *Butt v. Monteaux*, 1 K. & J. 98, since such acts. See also *Colt v. Woolaston*, 2 P. Wms. 153, where there was fraud; *Green v. Barrett*, 1 Sim. 45; *Williams v. Page*, 24 Beav. 654; *Blain v. Agar*, 1 Sim. 37; 2 Id. 289; *Cridland v. De Mauley*, 1 De G. & S. 459; *Hallows v. Fermie*, 3 Ch. 467; *Grand Trunk, &c., R. Co. v. Brodie*, 9 Hare, 822.

³ 1 *Lindley on Partnership* (4th ed.), 121, citing *Baird v. Ross*, 2 McQueen, 68; *Garwood v. Ede*, 1 Ex. 264; *Watts v. Salter*, 10 C. B. 477; *Vane v. Cobbold*, 1 Ex. 798; *Atkinson v. Pocock*, Id. 796; *Willey v. Parratt*, 3 Ex. 211; *Clements v. Todd*, 1 Ex. 286; *Jones v. Harrison*, 2 Ex. 52; *Oldham v. Brown*, 7 E. & B. 164; 2 E. & E. 398.

⁴ *Great Falls & C. R. R. Co. v. Copp*, 38 N. H. 124 (1859); *State v. Morristown Fire Ass'n*, 3 Zab. 195 (1851); *Morley v. Thayer*, 3 Fed. Rep. 737 (1880); *Chase v. Lord*, 77 N. Y. 1 (1879); *Slee v. Bloom*, 19 Johns. 453, 473 (1822); *Shaw v. Boylan*, 16 Ind. 384; *Coffin v. Rich*, 45 Me. 511 (1858); *Gray v. Coffin*, 63 Mass. 192, 199 (1852); *French v. Teschmaker*, 24 Cal. 518, 540; *Inhabitants of Norton v. Hodges*, 100 Mass. 241 (1868); *Oliver v. Liverpool & L. L. & F. Ins. Co.*, 100 Mass. 531, 539 (1868), holding that in order to prevent this limited liability the English Parliament expressly declared joint-stock companies not to be corporations. *Myers v. Irwin*, 2 Serg. & R. 371 (1816), the court saying: "The personal responsibility of the stockholders is inconsistent with the nature of a body corporate."

ates by implication this limited liability of its members. For this reason the statutes regulating joint-stock companies are frequently careful to state that nothing therein contained shall give such companies the character of corporations.¹ The older text books and the earlier reports did not emphasize or probably appreciate the vitality of this principle of law. Of such importance is it that it would seem to be the the great and distinguishing characteristic of corporations, and not a subsidiary or unimportant one. It seems to have been assumed rather than established by direct adjudication.² In the early turnpike company cases of New England a contrary rule seems to have been assumed, and the subscriber appears to have been open to assessments indefinitely, except that he might forfeit his stock.³ Such companies however, had no fixed par value of their stock. At present the rule of non-liability at common law, beyond the par

Liverpool Ins. Co. v. Massachusetts, 10 Wall. 566, 575 (1870); New Eng. Bk. v. Stockholders of N. S. Factory, 6 R. I. 188 (1859); Walker v. Lewis, 49 Texas, 123 (1878); Green v. Beckman, 59 Cal. 545 (1881); Jones v. Jarman, 34 Ark. 323 (1879); Windham Prov. Inst. v. Sprague, 43 Vt. 502 (1871); Woods v. Hicks, 7 Lea (Tenn.), 40, on the ground that the corporate creditor contracts not with the stockholders, but with the corporation. Terry v. Little, 101 U. S. 216 (1879), the court saying: "The individual liability of stockholders in a corporation is always a creature of statute. It does not exist at common law." Smith v. Huckabee, 53 Ala. 191 (1875), where the court said: "Immunity from such liability is one of the inducements which has led to the multiplication of private corporations, and caused them to supersede, to a great extent, in hazardous enterprises, or enterprises requiring large capital, partnerships." Spense v. Iowa Valley Construction Co., 36 Iowa, 407 (1873), the court saying: "It is one of the distinguishing features of incorporation that the individual property of its members may be exempt from liability for corporate debts. Therein consists the great superiority of a corporation over a partnership or an unincorporated joint-stock company." Salt Lake City Nat. Bk. v. Hendrickson, 40 N. J. L. Rep. 52 (1878); Van Sandan v. Moore, 1 Russ. Ch. 392, 408 (1826); Atwood v. Rhode I. Agri. Bk., 1 R. I. 376 (1850), the court

saying; "At common law the stockholders in a corporation are not liable individually for the corporate debts. The capital stock is the fund to which alone the creditors must resort, unless in cases of fraud." The case Atlantic De Laine Co. v. Mason, 5 R. I. 463 (1858), holds that the payment of one invalid assessment is no waiver of the right to object to another. Cf. Field v. Pierce, 102 Mass. 253 (1869).

¹ Oliver v. Liverpool, &c., Ins. Co., *supra*; Laws of N. Y., 1854, ch. 245, § 3, and see Chap. XXIX.

² In the case Carr v. Iglehart, 3 O. St. 457 (1854), the court took counsel to task for questioning this principle of law. The court said, it is contended "that stockholders in a corporation are individually liable for its debts, unless by some provision of the charter, or statute law, they are exempted from such responsibility. The counsel for the complainant admits that Blackstone and divers other eminent writers upon the law and also certain courts, have entertained a contrary opinion, but he is very clear that they were all wrong, and he hopes and thinks this court will not be governed by such loose and inconsiderate expressions, either of text books or judges." But counsel is wrong. "We suppose that no law is better settled than that they are not liable."

³ Middlesex Turnpike Co. v. Swan, 10 Mass. 384.

value of the stock, is established beyond question, and forms the chief inducement in the formation of the many corporations of the day.

§ 242. Attempts have been made in various ways to authorize the assessment of stockholders for amounts after the par value of their stock has been paid in. Such efforts have generally failed. It cannot be done by a majority vote of the stockholders, nor of the directors, nor by a by-law.¹ The liability is sometimes created by statute.² Where the State has reserved the power to alter, repeal, or amend the charter, it may authorize the corporation to levy assessments on its stockholders, in addition to the subscription of their stock. The reasoning of this rule is clear. The limited liability is a part of the corporate privileges conferred. A right to repeal the franchises includes the right to repeal in part or altogether the franchise or privilege of limited liability. On such grounds, laws of this character, however harsh in their operation, are upheld as constitutional.³

§ 243. *Miscellaneous cases of liability or non-liability.*—It has been held on grounds of public policy, that although a corporation is advertised as having a capital stock of a fixed amount, the shareholders and directors are not liable personally, even though

¹ Flint v. Pierce, 54 Mass. 539 (1868); Kennebec & Portland R. R. Co. v. Kendall, 31 Me. 470 (1850); Trustees of Free School v. Flint, 54 Mass. 539 (1847); Reid v. Eatonton Mfg. Co., 40 Ala. 98 (1869). In the first mentioned case the defendant subscribed to such a by-law, among other by-laws, when he subscribed for stock. Placing the words "individual property of stockholders liable" on the face of corporate liabilities has no effect in itself. Stockholders are liable only as prescribed by law. Lowry v. Inman, 46 N. Y. 119 (1871). The case, however, of Hume v. Winyah & W. Canal Co., Carolina Law Journal, 217, held, at an early day, that where a corporation, not professing to have any fixed capital, made a by-law by which each of the corporators were bound to contribute equally or ratably to all expenses incurred, the corporators were liable personally.

² In California, under sections 331, 333, of the Civil Code, a corporation may

assess its members to any extent, "for the purpose of paying expenses, conducting business, or paying debts." Santa Cruz R. R. Co. v. Spreckles, 65 Cal. 193 (1884). A better construction of such a statute prevails in Vermont. Under a charter provision that "if at any time the stock paid into said corporation shall be impaired by losses or otherwise, the directors shall forthwith repair the same by assessment," a receiver was not allowed to assess, since the provision is only to prevent a continuance of business with an impaired capital. Dewey v. St. Albans Trust Co., 59 Vt. 332 (1886). In Pennsylvania it is held that though the corporation has power to assess beyond the par value of the stock, yet such power may be restricted by by-law. Price's Appeal, 106 Pa. St. 421 (1884).

³ Gardner v. Hope Ins. Co., 9 R. I. 194 (1869); Meadow Dam Co. v. Gray, 30 Me. 547 (1849).

subscriptions have not been taken to that amount. They are not liable either for the untaken stock, or on the ground of false representations, since the capital stock is understood to represent what the corporation hopes to obtain in subscriptions.¹ An oral promise to pay corporate debts is void by the Statute of Frauds.² Partners, by becoming incorporated, do not thereby cease to be partners as to all the debts of the former partnership.³ A stockholder is not liable as a partner by reason of misrepresentations that the corporation is solvent, though probably he would be liable in damages for false representations.⁴ Upon the dissolution of the corporation the liability of the stockholder ceases. If the business is carried on thereafter by the agents, no liability therefor attaches to the former stockholders,⁵ unless they expressly authorize it.⁶ Persons who purchase a railroad at an execution sale thereof cannot continue to run it in the name of the old railroad corporation, and thereby be protected from liability as partners.⁷ They do not succeed to its corporate character, although they purchase its property. In all cases, however, in which the members of an association might have been held liable as partners, the right of the creditor to enforce that liability is barred by his bringing suit and obtaining judgment against the supposed corporation.⁸

¹ *First Nat'l Bk. v. Almy*, 117 Mass. 476 (1875); *Wakeman v. Dalley*, 51 N. Y. 27, 30; *Evans v. Coventry*, 25 L. J. (Ch.) 489 (1856); *Crease v. Babcock*, 51 Mass. 525, 557 (1846). *Contra*, *Haslett v. Wotherspoon*, Strob. Eq. (S. C.) 209, 229 (1847). In Illinois there is a statutory liability in a case like this. Stat. of Ill. ch. 32, s. 18.

² *Trustees of Free School v. Flint*, 54 Mass. 539 (1868).

³ *Broyles v. McCoy*, 5 Sneed. (Tenn.) 602 (1858). The case of *Martin v. Fewell*, 79 Mo. 401, 412 (1883), holds also that "for the debts incurred after they become a corporation, their liability will depend upon the fact of actual notice of

their incorporation to the plaintiffs at the time such debts were incurred."

⁴ *Searight v. Payne*, 2 Tenn. Ch. 175.

⁵ *Central City Sav. Bk. v. Walker*, 66 N. Y. 424 (1876), *aff'd* 5 Hun, 34.

⁶ *Nat'l Union Bk. of Watertown v. Landon*, 45 N. Y. 410 (1871).

⁷ *Chaffe v. Ludeling*, 27 La. Ann. 607 (1875).

⁸ *Cresswell v. Oberly*, 17 Brad. (Ill.) 281 (1885); *Pochelu v. Kemper*, 14 La. Ann. 308 (1859). The partners herein cannot bring an action at law against each other. Their remedy is in equity. *Crow v. Green*, 17 W. N. C. 409 (Penn. 1886). See also Chapter on Joint Stock Companies.

CHAPTER XIV.

LIABILITY OF TRUSTEES, EXECUTORS, AGENTS, &c.

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| <p>§ 244. The liability of trustees, executors, pledgees, &c.</p> <p>245. The apparent, though not the real owner of shares, is liable alike to the corporation and to corporate creditors.</p> <p>246. The liability of a trustee of stock.</p> <p>247. The liability of a pledgee of shares.</p> <p>248. The liability of an executor or administrator.</p> <p>249. The liability of an agent as transferor or transferee.</p> | <p>§ 250. The liability of infants and married women as transferrers or transferees.</p> <p>251. The liability of the corporation itself.</p> <p>252. The liability of legatees, assignees in insolvency, and joint owners of shares.</p> <p>253. The liability upon nominal and fictitious transfers.</p> |
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§ 244. *The liability of trustees, executors, pledgees, &c.*—

Where the apparent owner of shares is not the real owner, the registered title to the stock being in one person, and the equitable or real ownership being in another, various intricate questions have arisen involving the matter of liability for unpaid subscriptions, and liability under the statute. The cases, which are very numerous, present every variety of ownership, and every phase of liability, including many instances of transfer for the purpose of avoiding liability. Yet, although the principles and rules of law governing this branch of the subject are somewhat numerous and complicated, they are, nevertheless, comparatively well settled.

§ 245. *The apparent, though not the real owner, is liable alike to the corporation and to corporate creditors.*—A person in whose name stock is recorded on the corporate books, is liable on such stock, as though he were the absolute and legal owner, although, as a matter of fact, he holds stock which belongs to another.¹

¹ Mitchell's Case, L. R., 9 Eq. 363 (1870); King's Case, L. R., 6 Chan. 196 (1871); Newry, &c., R. R. Co. v. Moss, 14 Beav. 64 (1851); Shipman's Case, L. R., 5 Eq. 219 (1868); Buchan's Case, L. R., 4 App. Cas. 549 (1879); Chapman & Barker's Case, L. R., 3 Eq. 361 (1866); William's Case, L. R., 1 Chan. Div. 576 (1875); Hoare's Case, 2 John. & H. 229 (1862); Leifchild's Case, L. R., 1 Eq. 231 (1865); Adderly v. Storm, 6 Hill, 624 (1844); Mann v. Currie, 2 Barb. 294 (1848); Worrall v. Judson, 5 Id. 210 (1849); Roosevelt v. Brown, 11 N. Y. 148 (1854); Matter of the Empire City Bank, 18 Id. 199, 225 (1858); Crease v. Bab-

This rule is based on a wise public policy which protects corporate creditors and the corporation itself against transfers which seem to convey complete title, while in reality the transferee has but an equitable title. He who assumes the appearance of a real owner is obliged to bear the burdens of real ownership. As regards the corporation itself, it is a serious question whether it is obliged to enter upon its corporate books the fact that a transferee holds as a pledgee, or in some other special capacity. It undoubtedly is obliged so to do, when the transferee requests registry on the corporate books as a trustee of the stock.¹

§ 246. *Liability of trustee.*—A trustee of stock, who is recorded on the corporate books as a stockholder is, it seems, at common law, liable on such shares, as though he were the absolute owner of the same. This appears to be the rule, even though he is recorded on the corporate books, not as an absolute owner, but as a trustee of the stock.

The law requires that liability should attach to some one for every share of stock that is issued.² And to such an extent is this principle of law insisted on that the liability of the trustee is not limited by the amount of the trust property.³ In the case of two or more trustees, the liability is that of joint owners, and each is liable for the whole, and not *pro rata*, and where there is a single trustee he is liable primarily and simply to the

cock, 10 Metc. 525 (1846); *Grew v. Breed*, 10 Id. 569 (1846); *Holyoke Bank v. Burnham*, 11 Cush. 183 (1853). In *Shipman's Case*, L. R., 5 Eq. 219 (1868), where one transferred his shares to an irresponsible person, and the transfer was not registered, it was held that, upon the winding up, the transferrer must contribute, but that if the transferee had been solvent it would have been otherwise. In *Cutting v. Damerel*, 88 N. Y. 410, 415 (1882), the rule that entries in the corporate books are conclusive as to the ownership of shares as against corporate creditors was essentially qualified, and the earlier New York cases, cited *supra*, limited and distinguished, so that it cannot now be said that the rule as laid down in the text is, in the absence of statutory provisions, the common law rule in New York.

¹ See Ch. XIX. In England, the corporation is not bound to recognize the

stockholder as a trustee in respect of his shares, even though he be described as such in the corporate books. *Muir v. City of Glasgow Bank*, L. R. 4 App. Cas. 337 (1879). *Cf. Hemming v. Maddick*, L. R., 9 Eq. 175 (1870); *Ex parte Oriental Commercial Bank*, L. R., 3 Chan. 791 (1868); *Holt's Case*, 1 Sim. (N. S.) 389 (1851); *Ind's Case*, L. R., 7 Chan. 485 (1872).

² *Bransom v. Oregonian Ry. Co.*, 10 Oreg. 278; *Henkle v. Salem Mfg. Co.*, 39 O. St. 547; *William's Case*, L. R., 1 Ch. D. 576; *Sichell's Case*, L. R., 3 Ch. 119; *Bugg's Case*, 2 Dr. & Sm. 452.

³ *Chapman's Case*, L. R., 3 Eq. 361 (1866); *Leifchild's Case*, L. R., 1 Eq. 281 (1865); *Hoare's Case*, 2 John. & H. 229 (1862); *Muir v. City of Glasgow Bank*, L. R., 4 App. Cas. 337 (1879); *Grew v. Breed*, 10 Metc. 569 (1846). *Cf. Sales v. Bates*, 6 East. Rep. 703 (R. I. 1886).

full extent of the liability.¹ However, although it is the policy of the law to impose upon trustees the full liability, it is held that a trustee may accept the transfer with a stipulation that he is not to be charged as owner, and such a stipulation will be enforced.² It is well established that the *cestui que trust*, or beneficiary, cannot be charged in respect of the shares, either by the corporation or by the corporate creditors, when the stock stands on the corporate register in the name of a trustee.³ But the trustee who has been compelled to meet a charge upon the stock held by him as trustee, may have recourse to the amount of his expenditure from the *cestui que trust*.⁴

§ 247. *The liability of a pledgee of shares.*—A pledgee of stock, that is, one to whom the stock has been transferred in pledge or as collateral security, and who has had the stock transferred into his own name on the corporate books, is liable to the creditors of the corporation as though he were the absolute owner of the stock.⁵ This rule has frequently been enforced in

¹ *Cunninghame v. City of Glasgow Bank*, L. R., 4 App. Cas. 607 (1879); *Griswold v. Seligman*, 72 Mo. 110 (1880). In New York, however, by statute, in the case of shares in railway and manufacturing corporations, trustees in possession of shares are released from this liability, and the trust estate is expressly charged. Session Laws, 1850, chap. 140, § 11; *Idem*, 1848, chap. 40, § 13. And there is a like provision in the Revised Statutes of the United States, §§ 5151, 5152, in favor of trustees of shares of stock in the National Banks. *Davis v. Essex Baptist Society*, 44 Conn. 582 (1877); *Irons v. Manufacturers National Bank*, 6 Biss. 301 (1884).

² *Saunders's Case*, 2 De G., J. & S. 101 (1864); *Gray's Case*, L. R., 1 Chan. Div. 664 (1876); *In re City Terminus Hotel Co.*, L. R., 14 Eq. 10 (1872). Cf. *Chapman & Barker's Case*, L. R., 3 Eq. 361 (1866).

³ *Ex parte Bugg*, 2 Drew. & Sm. 452; *William's Case*, L. R., 1 Chan. Div. 576 (1875); *Sichell's Case*, L. R., 3 Chan. 119 (1867); *King's Case*, L. R., 6 Chan. 196 (1871); *Mitchell's Case*, L. R., 9 Eq. 363 (1870); *Newry, &c., R. R. Co. v. Moss*, 14 Beav. 64 (1851); *Shipman's Case*, L. R., 5 Eq. 219 (1868); *Hoare's Case*, 2 John. & H. 229 (1862). Cf. *Hemming v. Maddick*, L. R., 9 Eq. 175 (1870); *Fen-*

wick's Case, 1 De G. & Sm. 557 (1849). *In re National Financial Co.*, L. R., 3 Chan. 791 (1868); *James v. May*, L. R., 6 H. L. 328 (1873); *Cox's Case*, 4 De G., J. & S. 53 (1863); *Chinnock's Case*, John. (Eng. Chan.) 714 (1860); *Pugh & Sharman's Case*, L. R., 13 Eq. 566 (1872); *Fanning v. Insurance Co.*, 37 Ohio St. 339 (1881).

⁴ *James v. May*, L. R., 6 H. L. 328 (1873); *Hemming v. Maddock*, L. R., 7 Chan. App. 395 (1872); *Cruse v. Paine*, L. R., 6 Eq. 641 (1868); *Butler v. Cumpston*, L. R., 7 Eq. 16 (1868); *Mitchell's Case*, L. R., 9 Eq. 363 (1870); *Ex parte Oriental Commercial Bank*, L. R., 3 Chan. 791 (1868); *Hughes—Hallett v. Indian Mammoth, &c., Co.*, L. R., 22 Chan. Div. 561 (1882); *Hoare's Case*, 2 John. & H. 229 (1862). See also *Shaw v. Fisher*, 5 De G., M. & G. 596; *Evans v. Wood*, L. R., 5 Eq. 9; *Hawkins v. Maltby*, L. R., 4 Ch. 200; *Morris v. Cannan*, 4 De G., F. & J. 581; *Wynne v. Price*, 3 De G. & Sm. 310; *Kellogg v. Stockwell*, 75 Ill. 68; *Cheale v. Kenward*, 3 De G. & J. 27. As to the liability for charges on the stock upon the winding up, see *Re National Financial Co.*, L. R., 3 Chan. 791 (1868).

⁵ *Moore v. Jones*, 3 Woods, 53 (1877); *Pullman v. Upton*, 96 U. S. 328 (1877); *Crease v. Babcock*, 10 Metc. 525 (1846); *Holyoke Bank v. Burnham*, 11 Cush. 183

the case of a pledge of shares of stock in a national bank.¹ But there seems to be a tendency to limit its application, and to allow a pledgee, under proper limitations, to hold shares as security for his debt, without assuming any liability on the stock as owner.²

(1853); *Johnson v. Somerville Dyeing, &c., Co.*, 15 Gray, 216 (1860); *Melvin v. Lamar Insurance Co.*, 80 Ill. 446; *Adderly v. Storm*, 6 Hill, 624 (1844); *Rosevelt v. Brown*, 11 N. Y. 148 (1854); *Matter of The Empire Bank*, 18 Id. 199 (1858); *Grew v. Breed*, 10 Metc. 569 (1846); *Price & Brown's Case*, 3 De G. & Sm. 146 (1850); *Addison's Case*, L. R. 5 Chan. 294 (1870); *Royal Bank of India's Case*, L. R. 7 Eq. 91 (1868); s. o. L. R. 4 Chan. 252 (1869); *Weikersheim's Case*, L. R. 8 Chan. 831 (1873). Cf. *Richardson v. Abendroth*, 43 Barb. 162 (1864). For the rule in Louisiana see *Haynes v. Palmer*, 13 La. Ann. 240 (1858). And the pledgee is liable upon the stock even after the debt has been paid and the certificate handed back to the pledgor, if the retransfer is not properly entered on the corporate books. *Bowdell v. The Farmers & Merchants' National Bank of Baltimore*, 25 Nat. Bank. Reg. 405 (1877).

¹ *Magruder v. Colston*, 44 Md. 349 (1875); *Wheelock v. Kost*, 77 Ill. 296 (1875); *Hall v. Walker*, 31 Iowa, 344 (1871); *Barre National Bank v. Hingham Manfg. Co.*, 127 Mass. 563 (1879); *National Bank v. Case*, 99 U. S. 628 (1878). Upon this general question as affecting a pledge of shares in a national bank, see *Dickinson v. Central National Bank*, 129 Mass. 279 (1880); s. c. 37 Am. Rep. 351, and the learned annotation by Mr. Irving Browne. As to what passes title in such a pledge of shares, see *Koons v. First Natl. Bank of Jeffersonville*, 89 Ind. 178.

² Thus we find in New York that the General Railroad Act of 1850 provides that no person who holds stock in the railway corporations of that State as collateral security, shall be personally liable as a shareholder, but that such liability shall attach exclusively to the person who owns and has pledged the shares. New York Laws of 1850, chap. 140, § 11. See *McMahon v. Macy*, 51 N. Y. 155 (1872). Cf. *Guest v. Worcester, &c., Ry. Co.*, L. R. 4 C. P. 9. A similar provision is found in the New York Manufacturing Companies Act of 1848. New York Laws of 1848, chap. 40, § 16.

See *Stover v. Flack*, 30 N. Y. 64 (1864); s. c. 41 Barb. 162. Cf. *Case of the Reciprocity Bank*, 22 N. Y. 9, 17 (1860). And a similar provision has been enacted in Maryland. *Matthews v. Albert*, 24 Md. 527. In Missouri, however, it is held that the act does not operate to discharge a person to whom shares have been originally issued by the corporation as collateral security for money advanced to it. *Griswold v. Seligman*, 72 Mo. 110 (1880). In *Burgess v. Seligman*, 107 U. S. 20 (1882), the Supreme Court of the United States declined to put that construction upon the Missouri statute, and held that the pledgees were not liable to corporate creditors upon the shares so held by them. See also *Melvin v. Lamar Ins. Co.*, 80 Ill. 446 (1875); *Wheelock v. Kost*, 77 Ill. 298. In England, *Chapman's, &c., Case*, L. R. 3 Eq. 365; *Re Anglesea Colliery Co.*, L. R. 2 Eq. 379; *Inds' Case*, L. R. 7 Ch. 485, were under the Companies Act. In a late Massachusetts case it is said that the pledgee is liable on the stock as owner only when the certificate fails to show that the shares are held merely as collateral. *Barre National Bank v. Hingham Manfg. Co.*, 127 Mass. 563 (1879); s. r. *Davis v. Essex Baptist Society*, 44 Conn. 582 (1877). Upon the question of the responsibility of the several parties to the transaction when one who holds certificates of shares in his own name as "trustee," pledges the stock as security for his own debt, see *Shaw v. Spencer*, 100 Mass. 382 (1868). Mr. Justice Strong, in *National Bank v. Case*, 99 U. S. 628, 631 (1878), said: "It is thoroughly established that one to whom stock has been transferred in pledge, or as collateral security for money loaned, and who appears on the books of the corporation as owner of the stock, is liable as a stockholder for the benefit of creditors. . . . For this several reasons are given. One is that he is estopped from denying his liability by voluntarily holding himself out to the public as the owner of the stock, and his denial of ownership is inconsistent with the representations he has made; another is that by taking the legal title he has re-

§ 248. *The liability of an executor or administrator.*—The estate of a deceased person is liable upon the stock held and owned by the decedent in the same way and to the same extent that the shareholder was liable in his lifetime. Accordingly an executor or administrator of the estate of a deceased shareholder is chargeable upon the shares of the decedent to the extent of the property that comes into his hands, as the personal representative of the deceased.¹ The executor or administrator becomes personally liable, however, upon the stock, if he pay away the assets of the

leased the former owner; and a third is that, after having taken the apparent ownership, and thus become entitled to receive dividends, vote at elections, and enjoy all the privileges of ownership, it would be inequitable to allow him to refuse the responsibilities of a stockholder." But in the later case of *Anderson, Receiver v. Philadelphia Warehouse Co.*, 111 U. S. 479 (1883), it is held that a pledgee of shares of stock in a national bank, who in good faith, and with no fraudulent intent, takes the security for his benefit in the name of an irresponsible person, as trustee, for the avowed purpose of avoiding individual liability as a shareowner, and who exercises none of the rights or powers of a shareholder, incurs no liability which can be enforced by creditors of the bank in case of its failure. *Anderson v. Philadelphia Warehouse Co.*, 111 U. S. 479, 485 (1883). See also *Henkle v. Salem Manfg. Co.*, 39 Ohio St. 547 (1883). A transfer of shares by one who holds them merely as collateral security, for the purpose of avoiding liability thereon, is not a conversion. *Hiatt v. Griswold*, 5 Fed. Rep. 573 (1881); *Otis v. Gardner*, 105 Ill. 436. And in *Manchester Financial Corporation Company's Case*, 22 Week. Rep. 41 (1875), it is said that the holder of shares issued as fully paid up, merely as collateral security, cannot be held liable as though the holder of unpaid shares.

¹ *Thomas' Case*, 1 De G. & Sm. 579 (1849); *Baird's Case*, L. R. 5 Chan. 725 (1870); *Stewart's Trustee v. Evans*, 9 Scotch Ct. of Ses. Cas. (3d series), 810 (1871); *Evans v. Coventry*, 25 L. J. Chan. 489 (1856); *Blakeley's Case*, 13 Beav. 133 (1850); *Ex parte Gouthwaite*, 3 Mac. & G. 187 (1851); *Ex parte Doyle*, 2 Hall & Twell (Eng. Chan.) 221 (1850); *Ex parte Hall*, 1 Mac. & G. 307 (1849); *Hamer's Devisees' Case*, 2 De G., M. & G.

366 (1852); *Robinson's Executor's Case*, 6 Id. 572 (1856); *Ness v. Armstrong*, 3 De G. & Sm. 38, note (1849); *Buchan's Case*, L. R. 4 App. Cas. 549 (1879); *Hoare's Case*, 2 John. & H. 229 (1862); *Bulmer's Case*, 33 Beav. 433; *Gouthwaite's Case*, 3 De G. & Sm. 258 (1850); *Taylor v. Taylor*, L. R. 10 Eq. 477 (1870); *Alexander's Case*, 15 Sol. Jour. 788, (1871); *Hamer's Case*, 3 De G. & Sm. 279 (1850); *Grew v. Breed*, 10 Metc. 569 (1846); *New England Commercial Bank v. Stockholders of the Newport Steam Factory*, 6 R. I. 154 (1859); *Crandall v. Lincoln*, 52 Conn. 73 (1884); *Bailey v. Hollister*, 26 N. Y. 112 (1862); *Chas. v. Lord*, 77 Id. 1 (1879); *Witters v. Sawles*, 25 Fed. Rep. 168 (1885), relative to the liability of an executor under the Federal statute governing national banks. *Schouler on Executors*, § 380; *New York Laws of 1850*, chap. 140, § 11; 1848, chap. 40, § 13. Some of the earlier Massachusetts cases are in apparent conflict with the rule declared in the text. *Child v. Coffin*, 17 Mass. 64; *Gray v. Coffin*, 9 Cush. 200; *Ripley v. Sampson*, 10 Pick. 371; *Andrews v. Callender*, 13 Id. 484; *Dane v. Dane Manfg. Co.*, 14 Gray. 489; *Grew v. Breed*, 10 Metc. 569. In *Buchan's Case*, L. R. 4 App. Cas. 549, 588 (1879), the court said: "An executor whose testator has held shares in a joint-stock company, has generally one of two courses open to him. He may have the shares transferred into his own name and become to all intents and purposes a partner in the company. He may, on the other hand, not wish to have the shares transferred into his name, and he ought in that case to have a reasonable time allowed him to sell the shares and to produce a purchaser who will take a transfer of them." See also *Re Cheshire Banking Co.*, 54 L. T. Rep. 558 (1886).

estate in legacies without making provision to meet the liability on the stock.¹ When the executors accept a transfer in their own names they make themselves personally liable on the stock.²

§ 249. *The liability of an agent as transferrer or transferee.*

—Sometimes a subscription for stock is made by one person as the agent of another, and the stock is entered on the corporate books in the name of the agent. In such a case it is the rule that corporate creditors may hold either the principal or the agent responsible on the stock.³ But an agent who is compelled to assume and pay charges on the stock may recover from his principal the amount so paid.⁴ Where a transfer is made, not to the principal himself, but to an agent, the latter is but a nominal holder, and is subject to the rules applicable to such. The transferee of an agent, when suit is brought by corporate creditors, to enforce a demand against the stock, cannot set up that the agent had no power to transfer the stock to him. If he has received the certificates and appears as a stockholder on the books of the corporation, he is, as between himself and creditors of the corporation, a shareholder.⁵

§ 250. *The liability of infants and married women as transferrers or transferees.*—It has already been shown that an infant cannot be held liable upon a subscription to stock,⁶ and any per-

¹ Taylor v. Taylor, L. R. 10 Eq. 477 (1870); Jefferys v. Jefferys, 24 L. T. Rep. (N. S.) 177 (1871). In Stewart's Trustees v. Evans, 9 Scotch Ct. Ses. Cas. (3d series) 810 (1871), it is held that where executors pay away the estate *bona fide*, they are not, after a lapse of sixteen years, liable personally for a deficit on shares. Cf. Witters v. Sawles, 25 Fed. Rep. 168 (1885). An executor who accepts for the estate new shares, which the corporation offers upon specified conditions to the holders of its stock, even though it be done for the benefit of the estate, and in good faith, makes himself personally liable for any charge to the estate growing out of the ownership of such new or additional shares, and he cannot indemnify himself out of the funds of the estate for any loss he may sustain thereby in his individual capacity. Fearnside & Dean's Case, L. R. 1 Chan. 231 (1866); Spence's Case, 17 Beav. 203 (1853); Jackson v. Turquand, L. R. 4 H. L. 305 (1866); Mallorie's Case, L. R. 2 Chan. 181

(1867). Cf. Russell's Executor's Case, 15 Sol. Jour. 790 (1871).

² Alexander's Case, 15 Sol. Jour. 788 (1871). In New York it is held that an action to charge an executor on the stock of the estate need not be joined with an action to enforce an individual subscription by the executor. Erie, &c., Ry. Co. v. Patrick, 2 Keyes, 256 (1865). A special Statute of Limitations applicable to executors will apply to an executor's liability on stock. Sales v. Bates, 6 East. Rep. 703 (R. I. 1886).

³ Burr v. Wilcox, 22 N. Y. 551 (1860); Stover v. Flack, 30 Id. 64 (1864). See also §§ 64, 65. Cf. Grangers Market Co. v. Vinson, 6 Oregon, 172.

⁴ Orr v. Bigelow, 14 N. Y. 556 (1856); affirming s. c. 20 Barb. 21 (1854).

⁵ Wakefield v. Fargo, 90 N. Y. 213 (1882). Upon the liability of agents or trustees in these cases, see Crandall v. Lincoln, 52 Conn. 73 (1884).

⁶ See § 63.

son subscribing for shares in the name of an infant renders himself personally chargeable thereon. So, likewise, when shares are assigned or transferred to infants as a contrivance to escape liability, the transferrer remains liable.¹ In such a case the transfer to the infant is a mere nullity, and the position of the parties is not thereby changed.² And this is the rule, as to an infant transferee, although the transfer was *bona fide*, and even in ignorance of the infancy of the transferee.³ The infant may, however, upon attaining his majority, ratify or acquiesce in a transfer of shares to him during his infancy and thereby render himself liable on the stock.⁴ The plea of infancy in these cases must, however, allege repudiation within a reasonable time after attaining majority.⁵

¹ Capper's Case, L. R. 3 Chan. 458 (1868); Mann's Case, *Id.* 459, note (1867); Weston's Case, L. R. 5 Chan. 614 (1870); Richardson's Case, L. R. 19 Eq. 588 (1875); Roman v. Fry, 5 J. J. Marsh. 634 (1831); Castleman v. Holmes, 4 *Id.* 1 (1830).

² Upon the winding up, unless the transferrer of shares can "show that at some time or other there was a transferee of his upon the register who could be made liable in respect of those shares," he is himself liable. Curtis' Case, L. R. 6 Eq. 455 (1868); Reid's Case, 24 Beav. 318 (1857). *Cf.* Mann's Case, L. R. 3 Chan. 459, note (1867).

³ Thus a broker purchasing shares for the account of an infant, was held liable as holder of the stock, not even his broker's agency availing to protect him. Ruchizky v. De Haven, 97 Penn. St. 202 (1881); Mann's Case, *supra*. In this case it seems that stock was registered in the name of a pledgee, and upon payment of the debt, the pledgee by order of the pledgor, transferred the shares into the name of a minor, not knowing, however, that he was transferring to a minor. Upon the winding up the pledgee was held a contributory, on the ground that it was not more the duty of the company than of the transferrer, to look into the matter of the age of one named as a transferee. And in Weston's Case, L. R. 5 Chan. 614 (1870), it is held that a transferrer is liable, in such a case, "even . . . where he was entirely innocent of [a fraudulent intent in] the transaction, and not aware that the shares were being transferred to a minor." In Nick-

alls v. Merry, L. R. 7 H. L. 530 (1875), a stock jobber was held liable, where, in a suit to recover calls on stock sold by him for the Stock Exchange, it turned out that the ultimate transferee of the shares was a minor, and his transferrer had, in consequence, been compelled to pay the calls.

⁴ Lumsden's Case, L. R. 4 Chan. 31 (1868). In this case, where an infant held stock for six months after attaining his majority, the stock having been transferred to him during his infancy, and then sold part of it, he was, upon a winding up, held to be a contributory, the court saying: "The transaction originally appears to have been voidable, not void, for a deed will pass an interest to an infant, even when coupled with a liability, if it be for his benefit to accept it." Accordingly, where an infant, after becoming of age, permits his name to remain on the registry as a shareholder, he is held to have ratified the antecedent transfer to him during his minority. Cork, &c., Ry. Co. v. Cazenove, 10 Q. B. 935 (1847).

⁵ Dublin, &c., Ry. Co. v. Black, 8 Exch. 181 (1852). *Cf.* Birkenhead, &c., Ry. Co. v. Pilcher, 5 Exch. 24 (1850). Where an infant transferee became of age ten months before the winding up, he was held liable as a contributory by acquiescence. Ebbett's Case, L. R. 5 Chan. 302 (1870). But in a case where the winding up came just before an infant transferee became of age, it was held that no affirmative repudiation was necessary, but that some distinct act of affirmation alone would avail to render him liable after majority.

What is a reasonable time within which the infant must repudiate the contract in order to escape chargeability, is in general, a question of law, and it will vary with the particular circumstances of each individual case. In general it is the rule that the transferee on coming of age must disaffirm promptly. Laches will bar his right to repudiate.¹

Wilson's Case, L. R. 8 Eq. 240 (1869). Where the winding up occurs just before or just after the infant transferee becomes of age, it is said that he need not expressly repudiate in order to escape liability "because he cannot tell whether the company intends to enforce their claim against him, and, therefore, he is not bound till some steps are taken to resist his being a shareholder in the company." Mitchell's Case, L. R. 9 Eq. 363 (1870).

It seems, also, that a repudiation during infancy may, under certain circumstances, avail to discharge an infant shareholder from liability to pay calls which are made after he attained the age of twenty-one years. Newry and Enniskillen Ry. Co. v. Coombe, 3 Exch. 565, 578 (1849). The court in speaking to this point, said: "He became a shareholder by contract during infancy, and during infancy he disaffirmed the contract; therefore, in my opinion, he ceased to be a shareholder liable to be sued for calls."

But where the infant transferee, coming of age after the winding up had been commenced, offered to affirm the contract, it was held that the liquidators might, in the interest of the creditors, refuse to accept the offer, and might instead hold the transferor liable. Symon's Case, L. R. 5 Chan. 298 (1870).

¹ In one English case we find it held that two years delay after coming of age is a ratification of the contract. Mitchell's Case, L. R. 9 Eq. 363 (1870), and in another case ten months is held sufficient. Ebbett's Case, L. R. 5 Chan. 302 (1870). While in a third case a lapse of three years was held not to amount to an affirmation of the contract. Hart's Case, L. R. 6 Eq. 512 (1868). In this case the infant shareholder came of age six months after the proceedings to wind up the company had been commenced. He was served with notice of these proceedings shortly before his majority. Two years after, a list of shareholders liable as contributors, which included his name, was filed, and a year later a notice of a call was

served on him. He resisted the collection of the amount of that call and, although his resistance was made three years after he came of age, the court held that he was liable. But after a repudiation of the contract on attaining majority, it is held that rendering aid in holding the transferor liable, is not a waiver by the infant of his formal repudiation of the transfer to him, of which the corporate creditors can take advantage, when for any reason they fail to make their claim against the vendor of the infant. Baker's Case, L. R. 7 Chan. 115 (1871). If a father transfers shares of stock to his minor son, though in good faith, he is, upon the winding up, liable upon the stock as though no transfer had been attempted, if the son repudiates the transaction. Litchfield's Case, 3 De G. & Sm. 141 (1850); Weston's Case, L. R. 5 Chan. 614 (1870). Cf. Roman v. Fry, 5 J. J. Marsh. 634 (1831). And a director in an incorporated company who induces his minor children to take stock in the company in their own names, is liable upon the winding up for a breach of trust, in case the children are still minors. *Ex parte Wilson* L. R. 8 Chan. 45 (1872). But if a father buy shares in the name and for the benefit of his son, who is a minor, and when the transfer is made informs the broker of the vendor of the minority of the transferee, the father, upon the winding up, is not liable on the stock, but, the transferee continuing a minor when the right of action accrues, the corporate creditors may look to the transferor. Maitland's Case, 38 L. J. Chan. 554 (1869). So also where the vendor of shares allows the certificate to be made to the minor son of his vendee, and the son upon attaining his majority repudiates the transaction, the vendor and not the vendee is liable upon the winding up. Hennessey's Case, 3 De G. & Sm. 191 (1850). But where a shareholder transferred to an infant, and this infant to another infant, who in his turn transferred to an adult capable of responding upon

No general rule can be laid down as regards the effect of a transfer of stock to a married woman. By the law of most of the States, she may contract as a *feme sole* in respect to her separate estate, and doubtless may become a transferee of stock.¹ In such cases she would also have power to transfer her stock without the consent of her husband.

§ 251. *The liability of the corporation itself.*—When the corporation becomes the purchaser of its own stock, and the shares, as is generally the case, are transferred into the name of a trustee for the corporation, it is the rule, both here and in England, that the trustee is personally liable in respect of all the shares so standing in his name.² The transferrer also, if he knew that the transferee took, as trustee for the corporation, is liable upon the stock.³ But when this knowledge is not imputable to the trans-

the stock, all the transfers having been duly registered, it was held that the last vendee was a contributory, and that the intermediate transfers could not be avoided. *Gooch's Case*, L. R. 8 Chan. 266 (1872). It seems, therefore, that the act of the infant in transferring shares is valid and effectual to pass the title, and to discharge himself from liability on the stock.

¹ See § 62; also *Johnson v. Gallagher*, 3 De G., F. & J. 494; *Mrs. Matthewman's Case*, L. R. 3 Eq. 781; *Luard's Case*, 1 De G., F. & J. 533; *Queen v. Carnatic R. Co.*, L. R. 8 Q. B. 299. In *Angus's Case*, 1 De G. & Sm. 560, the constitution of the corporation prevented such a transfer. See also *Matter of Reciprocity Bk.*, 22 N. Y. 9. In England the husband is liable on stock owned by his wife when he married her. *Burlinson's Case*, 3 De G. & Sm. 18; *Sadler's Case*, Id. 36; *White's Case*, Id. 157. But is liable only for subsequent liabilities of the company. *Kluht's Case*, Id. 210. See also *Butler v. Cumpston*, L. R. 7 Eq. 16, where the wife was a *cestui que trust*.

A husband has been held liable on stock which was given to his wife after their marriage by way of legacy, and was accepted by her. *Thomas v. City of Glasgow Bk.*, 6 Scotch Ct. of Sess. (4th series), 607 (1879). A married woman is herself liable for the statutory liability on stock, where she has power to be a stockholder. *Sales v. Bates*, 6 East. Rep.

703 (R. I., 1886). The case *Simmons v. Dent*, 16 Mo. App. 288 (1884), holds that under a statute whereby a married woman may become a stockholder, a transfer of stock from the husband to the wife is valid, and relieves him from liability on the stock the same as though he had transferred to any other person.

² *Wilson v. Proprietors of Central Bridge*, 9 R. I. 590 (1870); *Matter of the Empire City Bank*, 18 N. Y. 199, 226 (1858); *Allibone v. Hager*, 46 Penn. St. 48; *Crandall v. Lincoln*, 52 Conn. 73 (1884). Cf. *Sanger v. Upton*, 91 U. S. 56, 60 (1875). To the same effect are the English cases. *In re St. Marylebone Baking Co.*, 5 De G. & Sm. 21 (1849). *In re National Financial Co.*, L. R. 3 Chan. 791 (1868); *Chapman & Barker's Case*, L. R. 3 Eq. 361 (1866); *Ind's Case*, L. R. 7 Chan. 485 (1872); *Hoare's Case*, 2 Johns. & H. 229 (1862); *Ex parte Henderson*, 19 Beav. 107; *Eyre's Case*, 31 Beav. 177; *Munt's Case*, 22 Id. 55; *Richmond's Case*, 3 De G. & Sm. 96; *Walter's Case*, Id. 244; See also Chap. XIX.

³ *Lawe's Case*, 1 De G., M. & G. 421 (1852); *Nicol's Case*, 3 De G. & J. 387, 433 (1859); *Walter's Second Case*, 3 De G. & Sm. 244 (1850); *Daniell's Case*, 22 Beav. 43 (1856). Cf. *Johnson v. Laffin*, 5 Dill. 65 (1878); s. c. *Thompson Nat. Bank Cases*, 331; s. c. 103 U. S. 800 (1880); and particularly *Crandall v. Lincoln*, 52 Conn. 73 (1884).

ferrer, he is not liable.¹ Nor, of course, is he liable when the corporation has power, by charter or otherwise, to deal in its own shares.² Where the owner of stock transfers it directly to the corporation itself, without the intervention of a trustee, the transferrer is not released from his liability on the stock, but remains as fully chargeable as though no transfer had been attempted.³

§ 252. *The liability of legatees, assignees in insolvency, and joint owners.*—A legatee of shares of stock may, of course, if he thinks proper, decline to receive his testator's gift. But, if he accepts the legacy, it is well settled that, as specific legatee, he is bound to pay all calls made upon the stock after the decease of the testator.⁴ He must also pay all calls voted before, but not due and payable, in the regular course of business, until after the testator's death.⁵

An assignee of the estate of a bankrupt is not liable, personally or as assignee, upon the bankrupt's shares of stock. He is not bound, as assignee, to accept as part of the estate, property

¹ Hollway's Case, 1 De G. & Sm. 777 (1849); Nicol's Case, 3 De G. & J. 387 (1859); Johnson v. Laffin, 103 U. S. 800 (1880).

In the recent and very authoritative decision by the Supreme Court of Errors of Connecticut, in the case of Crandall v. Lincoln, 52 Conn. 73 (May Term, 1884), it is held—and in the judgment of the author upon sound grounds of justice and public policy—where a corporation, the capital of which was impaired, was buying in its own stock through an agent who did not disclose to the sellers the name of the party for whom he was buying, but where the sales were in fact direct to the corporation, that this arrangement did not protect the sellers, since they had in fact received money from the capital stock of the corporation, and were not only bound to make inquiry, but were bound to find out who was the transferee of their several shares, and that they were chargeable with the knowledge of the agent, who became their agent for the purpose of the sale and transfer.

² Grady's Case, 1 De G., J. & S. 488 (1863); Lane's Case, Id. 504 (1863). Sometimes, by agreement between discontented stockholders and the directors of the corporation, transfers are made by

such shareholders as desire to be released from their obligation as shareholders to nominees of the directors, with the intent thereby to relieve themselves from liability upon the stock. In such cases it is held that the action of the directors in permitting or sanctioning such a transfer was *ultra vires*, and that in consequence the transferrer is still liable. Morgan's Case, 1 De G. & Sm. 750 (1849); Bennett's Case, 5 De G., M. & G. 284 (1854). *In re Patent Paper Manfg. Co.*, L. R. 5 Chan. 294 (1870); Nathan v. Whitlock, 9 Paige, 152 (1841).

³ Case of the Reciprocity Bank, 22 N. Y. 9 (1860); Currier v. Lebanon Slate Co., 56 N. H. 262 (1875); Johnson v. Laffin, 5 Dill. 65 (1878); s. c. 6 Central Law Jour. 124; 103 U. S. 800 (1880); Walter's Second Case, 3 De G. & Sm. 244 (1850). Compare Zulusta's Claim, L. R. 5 Chan. 444 (1870); South Eastern Ry. Co.'s Claim, L. R. 14 Eq. 10 (1872); *In re Patent Paper Manfg. Co.*, L. R. 5 Chan. 294 (1870).

⁴ Day v. Day, 6 Jur. (N. S.) 365 (1860). Cf. Witters v. Sawles, 25 Fed. Rep. 168 (1885).

⁵ Addams v. Ferick, 26 Beav. 384 (1859). For a more complete statement of the law relative to legacies of stock, see Chap. XVIII.

of this nature, when it is of an onerous or unprofitable character.¹

Upon the death of one who is joint owner with another or others, of shares of stock, the liability thereon attaches only to the surviving owners, and the estate of the deceased owner cannot be charged.²

§ 253. *The liability upon nominal and fictitious transfers.*—Where one allows himself to be made the nominal owner of stock, that is to say, when one permits stock to be entered on the corporate books and the certificate to be issued in his name, when in reality he is not the actual owner of the stock, it is the well settled rule that he thereby renders himself liable as a stockholder to corporate creditors to the same extent that any *bona fide* stockholder is liable. He will not be heard to allege that he has perpetrated a fraud upon the creditors of the corporation by holding himself out as owner, when in fact he was not.³ It has been held, however, that in the case of a nominal ownership of stock, the object of the real owner being to escape liability, the law will disregard the nominal owner and will hold the real owner liable on the stock.⁴ Whenever it appears that the transferee of

¹ *American File Co. v. Garrett*, 110 U. S. 288 (1883); *Amory v. Lawrence*, 3 Cliff. 523; *Rugely & Harrison v. Robinson*, 19 Ala. 404; *Streeter v. Sumner*, 31 N. H. 542; *South Staffordshire Ry. Co. v. Burnside*, 3 Exch. 129; *Ex parte Davis*, L. R. 3 Chan. Div. 463; *Furdoonjee's Case*, Id. 268. And where a corporation itself assigned shares of its own stock to an assignee for the benefit of corporate creditors, it was held that the assignee was not liable, personally or as assignee, thereon. *In re City Terminus Hotel Co.*, L. R. 4 Eq. 10 (1872).

It has been held otherwise, however, in a case where the assignment was absolute, and the assignee was also a creditor. *Protection Life Insurance Co. v. Osgood*, 93 Ill. 69.

It has been held that one who makes an assignment for the benefit of creditors is thereby released from liability on stock, even though the transfer has not been recorded in the corporate books. *Sales v. Bates*, 6 East. Rep. 703 (R. I., 1886).

² *Re Maria Anna, &c.*, *Coal & Coke Co.*, 44 L. J. Chan. 423 (1875).

³ *Wakefield v. Fargo*, 90 N. Y. 213 (1882); *Case of the Reciprocity Bank*, 22 Id. 9 (1860); *Slee v. Bloom*, 19 John. 456 (1821); *Fisher v. Seligman*, 75 Mo. 13 (1881); *Griswold v. Seligman*, 72 Id. 110 (1880); *Ersine v. Lowenstein*, 11 Mo. App. 595 (1882); *Dane v. Young*, 61 Me. 160 (1872); *Wheelock v. Kost*, 77 Ill. 296 (1875); *Appeal of Miller*, 1 Penn. Sup. Ct. 120 (1881); *Graff v. Pittsburgh, &c.*, R. R. Co., 31 Penn. St. 489 (1858); *McHose v. Wheeler*, 45 Id. 32 (1863); *Aultman's Appeal*, 98 Id. 505 (1881); *National Bank v. Case*, 99 U. S. 628 (1878); *Price & Brown's Case*, 3 De G. & Sm. 146 (1850); *Barrett's Case*, 4 De G., J. & S. 416 (1864); *Straffon's Executor's Case*, 1 De G., M. & G. 576 (1852); *Gower's Case*, L. R. 6 Eq. 77 (1868). *Cf.* *Fox v. Clifton*, 6 Bing. (Eng.) 776 (1830).

Cases of this class are very similar in their character to cases of stock registered in the name of a trustee. The same rules of law apply to both classes of cases.

⁴ *Cox's Case*, 4 De G., J. & S. 53. *Cf.* *King's Case*, L. R. 6 Ch. 196. See also § 249.

shares is a fictitious and not a real person, the transferrer, or the real owner of the shares, will be held liable.¹ It is also held that such an assumed transfer is a mere nullity, and that the position of the parties is in no way changed thereby.²

¹ Pugh & Sharman's Case, L. R. 13 Eq. 566 (1872). Cf. Maitland's Case, 38 L. J. Chan. 554 (1869); Richardson's Case, L. R. 19 Eq. 588.

² Arthur v. Midland Ry. Co., 3 Kay & J. 204 (1857); Muskingum Valley Turnpike Co. v. Ward, 13 Ohio, 120 (1844). So where one purchased, or assumed to

purchase, shares for an infant, and took the certificate in the name of an imaginary person, it was held that by such a transaction the purchaser did not become liable upon the shares, nor was the vendor released. Maitland's Case, 38 L. J. Chan. 554 (1869).

CHAPTER XV.

LIABILITY AS AFFECTED BY TRANSFERS.

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| <p>§ 254. Liability upon transferred shares of stock.</p> <p>255. Liability of the transferrer on unpaid subscriptions.</p> <p>256. Liability of the transferee on unpaid subscriptions.</p> <p>257. Knowledge that the shares are not fully paid up, how far imputable to a transferee.</p> <p>258. Liability after transfer, but before registry.</p> <p>259. Liability of transferee to transferrer herein.</p> <p>260. At what time the statutory liability</p> | <p>for a debt attaches to the shares.</p> <p>§ 261. Transferrer not liable for debts incurred after the registry.</p> <p>262. Transferrer can claim exemption from liability for corporate indebtedness only after the registry of the transfer.</p> <p>263. The transferee's statutory liability.</p> <p>264. Liability of transferee to transferrer by way of indemnity.</p> <p>265. A transfer to an insolvent to escape liability.</p> <p>266. The rule in England.</p> |
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§ 254. *Liability upon transferred shares of stock.*—When shares of stock are transferred from one owner to another, or pass from the possession of one owner to that of another, it at once may become an important matter to determine, who is liable upon unpaid subscriptions, and who must assume the liability imposed by statute. The difficulty is increased by the rule of law that no transfer is complete until it is duly entered or recorded in the transfer book of the corporation. The complication is usually greatest in cases involving the question of statutory liability, since generally each case stands by itself in respect to the determination of this question, turning more or less upon the particular words of the statute by which the liability is imposed. There are, however, many rules which are general in their character and application, governing the liability of shareholders as affected by transfer, and these are the subject of this chapter.

§ 255. *Liability of the transferrer on unpaid subscriptions.*—Transfers of shares may be made at any time after the contract of subscription is made, and before any part, or after only a part of the subscription price has been paid. The well established and general rule of law in such cases is that where a stockholder makes an absolute transfer of his stock in good faith, and

the transfer is consummated by the record of the transfer in the corporate stock book, the transferrer is thereby wholly discharged from all further liability upon the unpaid subscription price of the stock. He is entirely absolved from any responsibility thereupon, whether part or nothing at all had been paid on the stock previously to the transfer.¹ This is the rule, although the corporate officers enter the transfer against the protest of the transferee.² But the transferrer is liable for calls payable before the transfer is made,³ and perhaps for calls made before, but payable after the transfer.⁴ Upon this latter point there can be no fixed and inflexible rule as to whether one, after a transfer of his shares, in good faith, to a solvent person, remains liable for calls

¹ *Johnson v. Laffin*, 5 Dill. 65 (1878) (by Dillon, J.); *Huddersfield Canal Co. v. Buckley*, 7 Term Rep. 36 (1796) (by Lord Kenyon); *Executors of Gilmore v. Bank of Cincinnati*, 8 Ohio, 62, 71; *Billings v. Robinson*, 94 N. Y. 415 (1884); affirming s. c. 28 Hun, 122 (1882); *Wakefield v. Fargo*, 90 N. Y. 213 (1882); *Cowles v. Cromwell*, 25 Barb. 413 (1857); *Cole v. Ryan*, 52 Id. 168 (1868); *Isham v. Buckingham*, 49 N. Y. 216 (1872); *Chouteau Spring Co. v. Harris*, 20 Mo. 382 (1855); *Miller v. Great Republic Ins. Co.*, 50 Id. 55; *Allen v. Montgomery R. R. Co.*, 11 Ala. 437, 451 (1847); *Haynes v. Palmer*, 13 La. Ann. 240 (1858); *Hartford, &c., R. R. Co. v. Boorman*, 12 Conn. 580 (1838); *Bend v. Susquehanna Bridge, &c., Co.*, 6 Harr. & J. 128 (1825); *Hall v. United States Ins. Co.*, 5 Gill (Md.), 484 (1847); *Webster v. Upton*, 91 U. S. 65 (1875); *Aylesbury Ry. Co. v. Mount*, 5 Scott's New. Rep. 127 (1842); *Weston's Case*, L. R., 4 Chan. 20 (1868); *McKenzie v. Kittridge*, 24 Upp. Can. C. P. 1 (1874). The mere fact that the transferrer, after the registry, paid a call does not estop him from denying his liability for subsequent calls. *Provincial Ins. Co. v. Shaw*, 19 U. C. (Q. B.) 533 (1860). Compare in general *Wintringham v. Rosenthal*, 25 Hun, 580 (1881); *Shellington v. Howland*, 53 N. Y. 371, 376 (1873); *Waterhouse v. Jamieson*, L. R., 2 Sc. App. 29 (1870); *Spargo's Case*, L. R., 8 Chan. 407 (1873). *In re Hoylake Ry. Co.*, L. R., 9 Chan. 257 (1874). It is not necessary to the validity of the transfer that there should be a consideration moving from transferee to transferrer, and so where one gives his share away absolutely and in good

faith, the same rule as to liability prevails. *In re European Bank*, Master's Case, 41 L. J. Chan. 501 (1872). Neither does it alter the rule that no certificates of stock have been issued, and that in consequence no certificates have been transferred. In such a case where the transaction is in good faith and absolute, the transferee equally becomes liable on the stock, and the transferrer's liability is at an end. *Burke v. Smith*, 16 Wall. 390 (1872); *Brigham v. Mead*, 10 Allen, 245 (1865); *Thorp v. Woodhull*, 1 Sandf. Chan. 411 (1844). See also *Upton v. Burnham*, 3 Biss. 431, 520 (1873); *First National Bank v. Gifford*, 47 Iowa, 575, 583. *Cf. Midland, &c., Ry. Co. v. Gordon*, 5 Railway & Canal Cases, 76 (1847); s. u. 16 Mee. & W. 804; *Isham v. Buckingham*, 49 N. Y. 216 (1872). See also *Shellington v. Howland*, 53 N. Y. 371, 376 (1873).

² *London, &c., Ry. Co. v. Fairclough*, 2 Man. & G. 674, 706 (1841); *Upton v. Burnham*, 3 Biss. 520 (1873); *Webster v. Upton*, 91 U. S. 65 (1875). In a proceeding in equity a transferee will be compelled to pay calls made after transfer of the certificate and before registry of the same. *Webster v. Upton*, *supra*.

³ *Vicksburg, &c., R. R. Co. v. McKean*, 14 La. Ann. 724 (1859).

⁴ *North American Colonial Association v. Bentley*, 19 L. J. (Q. B.) 427 (1850); *Schenectady, &c., Plank Road Co. v. Thatcher*, 11 N. Y. 102, 113 (1854). *Contra*, *West Philadelphia Canal Co. v. Innes*, 3 Wharton, 198 (1838); *Aylesbury Railway Co. v. Mount*, 4 Man. & G. 651; s. c. 5 Scott's New. Rep. 127 (1842).

made before the transfer, but becoming due and payable afterwards. The decision will generally depend either upon the terms of the contract between the transferrer and the transferee, or upon the express provisions of the statute under which the liability is imposed.¹

§ 256. *Liability of the transferee on unpaid subscriptions.*

—When a transfer of stock is made, and the transfer is duly recorded in the corporate stock book, the transferee thereupon becomes liable for any balance of the subscription price remaining unpaid at the time of the transfer. Since the transfer releases the transferrer it charges the transferee. The latter is in the situation of an assignee and assumes this liability of his assignor. Hence it is the well established rule that the transferee of shares is liable for calls made after he has been registered in the corporate transfer book as a stockholder, and being thus liable there is an implied promise that he will pay calls subsequently made upon the stock.² Under the rule in Pennsylvania, by which the trans-

¹ *Schenectady, &c., Plank Road Co. v. Thatcher*, 11 N. Y. 102. See *Morawetz on Corporations* (2d ed.), § 161; *Thompson on Liabilities of Stockholders*, § 210. In New York no stock in either railroad or manufacturing corporations, created by the laws of that State, can be lawfully transferred while there are calls unpaid upon the shares. N. Y. Session Laws, 1850, chap. 140, § 8; N. Y. Session Laws, 1848, chap. 40, § 8. So in California as to railroad stock, *Brewster v. Hartley*, 37 Cal. 15. In Tennessee it is held that upon a valid transfer, the transferrer is released, not only upon his liability for unpaid subscriptions, but also as to all the existing debts of the corporation, and this is the general rule. *Jackson v. Sligo Manfg. Co.*, 1 Lea, 210 (1878). So in Alabama, *Allen v. Montgomery R. R.*, 11 Ala. 437. But in Pennsylvania, by way of exception to the prevailing rule, the courts held an original subscriber to the capital stock of a corporation, formed under the General Railroad Act of that State of February 19, 1849, liable personally for any amount remaining unpaid upon the subscription, notwithstanding a transfer of the shares. The transfer is not allowed to operate to discharge the stockholder from his liability, although made in good faith, and although the transferee is solvent. *Pittsburgh, &c.,*

R. R. Co. v. Clarke, 29 Penn. St. 146 (1857); *Graff v. Pittsburgh, &c., R. R. Co.*, 31 Id. 489 (1858). *Cf. Frank's Oil Co. v. McCleary*, 63 Id. 317 (1839); *Messersmith v. Sharon Savings Bank*, 96 Id. 440 (1880); *Aultman's Appeal*, 98 Id. 505 (1881); *Pittsburgh, &c., Iron Co. v. Otterson*, 4 Week. Notes Cas., 545 (1878). In Maryland also the ordinary statutory provisions holding stockholders liable until the capital stock is fully paid in, is held to render the shareholder liable, even though he have transferred his shares. *Hager v. Cleveland*, 36 Md. 476 (1872). These anomalous decisions, however, are in general restricted to original subscribers and subsequent transferees are held to be discharged by a transfer. *West Philadelphia Canal Co. v. Innes*, 3 Wharton, 198 (1838); *Aultman's Appeal*, 98 Penn. St. 505 (1881); *Bunn's Appeal*, 105 Id. 49 (1884).

² *Webster v. Upton*, 95 U. S. 65 (1875); *Pullman v. Upton*, 96 Id. 328 (1877); *Upton v. Hansbrough*, 3 Biss. 417 (1873); *Foreman v. Bigelow*, 4 Cliff. 508 (1878); *Mann v. Currie*, 2 Barb. 294 (1848); *Cole v. Ryan*, 52 Id. 168 (1868); *Hall v. United States Ins. Co.*, 5 Gill (Md.), 484 (1847); *Bend v. Susquehanna Bridge Co.*, 6 Har. & J. 128, (1825); *Merrimac Mining Co. v. Bagley*, 14 Mich. 501 (1866); *Brigham v. Mead*, 10 Allen, 245

ferrer, if he be an original subscriber for shares, is not released from liability as to unpaid balances of subscription, it seems that the transferee incurs no liability in that respect, by the transfer. Inasmuch as the transferrer is not released the transferee is not charged.¹ Where by statute; or a by-law of the corporation, no valid transfer can be made while there are calls due and unpaid, it is held that a transfer without such payment will not render the transferee liable thereon.²

§ 257. *Knowledge that the shares are not fully paid up, how far imputable to a transferee.*—The question whether the purchaser of shares is bound to take notice that the stock he purchases is not fully paid for, is a serious and complicated one. The better opinion, and the one most in accord with the usages and analogies and demands of trade, is that, where one buys stock in open market, in good faith, without notice that the subscription price thereof has not been paid up, such a purchaser cannot be held liable to pay the unpaid balance of subscription.³

§ 258. *Liability after transfer, but before registry.*—Until a transfer is only recorded in the transfer book of the corporation, the transferee, not being duly recognized as a stockholder, is not chargeable either with corporate debts or unpaid balances of the

(1865); *Hartford, &c. R. R. Co., v. Boorman*, 12 Conn. 520 (1838); *Moore v. Jones*, 3 Woods, 53 (1877); *In re South Mountain, &c., Mining Co.*, 7 Sawyer, 30 (1881); *Merrimac Mining Co. v. Levy*, 54 Penn. St. 227 (1867); *Huddersfield Canal Co. v. Buckley*, 7 Term Rep. 36 (1796); *Evans v. Wood*, 37 L. J. Chan. 159 (1868). See also *Seymour v. Sturges*, 26 N. Y. 134 (1862).

¹ *Pittsburgh, &c., R. R. Co. v. Clarke*, 29 Penn. St. 146 (1875); *Messersmith v. Sharon Savings Bank*, 96 Id. 440 (1880); *Palmer v. Ridge Mining Co.*, 34 Id. 288; *Franks Oil Company v. McCleary*, 63 Id. 317 (1869); *Pittsburgh Iron Co. v. Otterson*, 4 Week. Notes Cas. 545 (1878); *Delaware Canal Co. v. Sansom*, 1 Binn. 70 (1803). *Cf.* *West Philadelphia Canal Co. v. Innes*, 3 Wharton, 198 (1838); *Merrimac Mining Co. v. Levy*, 54 Penn. St. 227 (1867); *Aultman's Appeal*, 98 Id. 505 (1881).

² *Watson v. Eales*, 23 Beav. 294 (1856); *McCready v. Rumsey*, 6 Duer, 574 (New York Super. Ct.) (1857), in a case under a

prohibition to transfer in articles of association of a bank, organized under the General Banking Act of 1838 of the State of New York. *In re Bachman*, 12 Nat. Bank. Reg. 223 (1875).

³ Certificates of stock have become such important factors in trade and credit, and general investment by all classes, that the law is steadily tending towards the complete protection of a *bona fide* purchaser of them in open market, and without notice of facts which will decrease the apparent value of the stock. The constant tendency of the courts to increase the negotiability of certificates of stock will probably, at some time hereafter, allow any liability on unpaid subscriptions to be enforced against a transferrer only when such liability is stated on the face of the certificate itself. At present, however, it would seem that a purchaser of the certificate is bound to inquire and know whether the stock is issued as paid up stock or not. See § 50.

subscription. Whatever may be his liability to the transferrer, he is not, until registry, liable either to the corporation or to corporate creditors upon any claim or demand growing out of the ownership of the shares transferred to him.¹ The transferrer is not released from liability until the transfer is duly registered in the corporate books.² The stock book of the corporation is kept largely for the purpose of informing the corporation and corporate creditors who the stockholders are and who is liable on the stock. Accordingly he in whose name the stock is registered at a particular time, is liable for obligations arising on the stock during that time.³

The corporation, after receiving and recognizing the transferee as a shareholder, cannot afterwards repudiate the transfer for informalities and hold the transferrer liable.⁴ And when the formalities of transfer are waived, either expressly or by plain implication, the transfer may be valid and operate to bind the transferee without any record of the transfer on the corporate books.⁵

¹ *Marlborough Manfg. Co. v. Smith*, 2 Conn. 579 (1818); *Louisiana Insurance Co. v. Gordon*, 8 La. Rep. 174 (1835); *Midland, &c. Ry. Co. v. Gordon*, 16 Mee. & W. 804 (1847). In Indiana it has been held that in no event will a statute be construed so as to make both transferrer and transferee liable directly for the same indebtedness. *Williams v. Hanna*, 40 Ind. 535 (1872).

² *Shellington v. Howland*, 53 N. Y. 371 (1873); *Worrall v. Judson*, 5 Barb. 210; *Dane v. Young*, 61 Me. 160; *Davis v. Essex, &c. Society*, 44 Conn. 582 (1877); *Kellogg v. Stockwell*, 75 Ill. 68; *Rosevelt v. Brown*, 11 N. Y. 148 (1854); *London, &c. Ry. Co. v. Fairclough*, 2 Man. & G. 674 (1841); *Humble v. Langston*, 7 Mee. & W. 517; *McEuen v. West London Wharves, &c. Co.*, L. R. 6 Chan. 655; *Sayles v. Blane*, 19 L. J. (Q. B.) 19; s. c. 6 Eng. Ry. Cases, 79. The liability as between transferrer and transferee after transfer and before registry is sometimes fixed precisely by statute. "No transfer of stock shall be valid for any purpose whatever, except to render the person to whom it shall be transferred liable for the debts of the company, according to the provisions of this act, until it shall have been entered therein [i. e., in the corporate stock book] as required by this section, by an entry showing to and from whom transferred."

New York Session Laws 1848, chap. 40, § 25. See, construing this section, *Heries v. Platt*, 13 Hun, 492 (1878); *Johnson v. Underhill*, 52 N. Y. 203 (1873).

³ It has been held, however, that so far as the unpaid subscription is concerned, there need not necessarily be a registry of the transfer, but that a recognition of the transferee as a stockholder by the corporation is sufficient. Thus in a late New York case, where it appeared that the stock was transferred by a blank endorsement, though not transferred on the corporate books, and dividends were paid to the transferee for a period of four years, the entries in the dividend book and in the corporate ledger being in their names, and the transferees having become corporate officers, it was held that the transferrers were not liable for unpaid subscriptions, and that an action by the receiver against them would not lie. *Cutting v. Damerel*, 88 N. Y. 410 (1882). *Of. Johnson v. Underhill*, 52 Id. 203 (1873). But *cf. Bosanquet v. Shortridge*, 4 Exch. 699 (1850).

⁴ *Isham v. Buckingham*, 49 N. Y. 216 (1872); *Cutting v. Damerel*, 88 Id. 410 (1882); *Chambersburg Ins. Co. v. Smith*, 11 Penn. St. 120 (1849); *Murray v. Bush*, L. R. 6 House of Lords, 37 (1873). *Of. Taylor v. Hughes*, 2 Jones & Lat. (Irish Chan.) 24.

⁵ *Upham v. Burnham*, 3 Biss. 431

§ 259. *Liability of transferee to transferrer herein.*—A transfer of stock may be said to involve three distinct acts, all of which may take place at one and the same time, or each at a different time. There is, first, the agreement of sale, by which the right to the stock passes from the transferrer to the transferee; second, the formal transfer of the certificate of stock; third, a registry of the transfer, by an entry on the corporate transfer book. It frequently happens that the registry is not made until some time after the agreement of sale, and that during the *interim*, calls on the subscription are made or corporate creditors' rights attached. The law then holds liable the transferrer whose transfer has not been registered. But in reality his transferee ought to meet that liability. Hence the rule that for liabilities arising after a sale of stock, but before a registry of the same on the corporate books, the vendee is liable to the vendor when such liabilities are paid by the latter.¹ The transferrer in these cases may have recourse to the real and not the nominal transferee.² In case of several successive transfers, the transferrer, who has paid an assessment or corporate debt, may look to his immediate transferee, although there be another one in the series who will ultimately be charged.³ In general the transferrer who has paid may seek his relief at law,⁴ or by a suit in equity.⁵

(1873). See also *Isham v. Buckingham*, 49 N. Y. 216 (1872); *Bernard's Case*, 5 De G. & Sm. 283 (1852). See note, *supra*.

¹ *Lord v. Hutzler*, 3 Atlantic Rep. 891 (1886); *Johnson v. Underhill*, 52 N. Y. 203 (1873); *Kellogg v. Stockwell*, 75 Ill. 68 (1874); *Hutzler v. Lord*, 64 Md. 534 (1885); *Brigham v. Mead*, 10 Allen, 245 (1865); *Walker v. Bartlett*, 18 C. B. 845, overruling *Humble v. Langston*, 7 Mee. & W. 517; *Chapman v. Shepherd*, L. R. 2 C. P. 228; *Grissell v. Bristowe*, L. R. 3 C. P. 112; *Davis v. Haycock*, L. R. 4 Exch. 373; *Bowring v. Shepherd*, L. R. 6 Q. B. 309; *Kellock v. Enthoven*, L. R. 9 Q. B. 241; s. c., L. R. 8 Q. B. 458. The Statute of Limitations does not begin to run against the transferrer until the assessment is paid by him. *Hutzler v. Lord*, *supra*. For cases relative to the transferrer's right to indemnity for statutory liabilities paid by him, see *infra*. So, also, when shares are sold for future delivery, but before the time for delivery the seller, in order to save the stock from forfeiture, is compelled to pay assess-

ments duly levied upon it, the seller may refuse to deliver until he is repaid the amount of such assessments. *Whitney v. Page* (N. Y. Super. Ct.), *Daily Register*, March 31, 1885.

² *Castellan v. Hobson*, L. R. 10 Eq. Cas. 47 (1870), but see *Shaw v. Fisher*, 2 De G. & Sm. 11 (1848); s. c. 5 De G., M. & G. 596 (1855).

³ *Kickalls v. Eaton*, 23 L. T. (N. S.) 689 (1871), or he may look to the final transferee, even though the call was made before the latter purchased. *Hawkins v. Maltby*, L. R. 3 Ch. 188 (1867).

⁴ See the cases generally cited in the preceding notes.

⁵ *Wynne v. Price*, 3 De G. & Sm. 310 (1849); *Cheale v. Kenward*, 2 De G. & J. 27; *Morris v. Cannan*, 4 De G., F. & J. 581; *Hawkins v. Maltby*, L. R. 4 Chan. 200 (1868); *Butler v. Cumpston*, L. R. 7 Eq. 16; *Evans v. Wood*, L. R. 5 Eq. 9 (1867); *Cruse v. Paine*, L. R. 6 Id. 641; s. c. 4 Id. 441; *Shaw v. Fisher*, 2 De G. & Sm. 11 (1848); s. c. 5 De G., M. & G. 596 (1855); *James v. May*, L. R. 6 House

§ 260. *At what time the statutory liability for a debt attaches to the shares.*—When the question of statutory liability is considered there is more difficulty, as between transferrer and transferee, in determining who is to be charged. Frequently the statute itself prescribes when the liability is to attach.¹ The most important question which arises herein, is whether the corporate debt raises a liability against him who was a stockholder when the corporation entered into the contract leading to the debt, or against him who was a stockholder when the debt itself became due and payable to the corporate creditor, or against him who was a stockholder when suit is brought by the corporate creditor against the corporation to collect the debt.² In certain cases it has been held that those shareholders would be held liable who were such at the time when the execution against the corporation was returned *nulla bona*.³

Many cases hold that where the individual liability of a shareholder is unlimited, and similar to that of a partner, in an unincorporated company, he will, while not liable for debts contracted before he became a shareowner, remain liable for all debts contracted during his membership, even though he may transfer his stock.⁴ Formerly in New York, and still, it seems, in California and Indiana, the exceptional rule prevails that the test of liability is whether the shareholder was such at the time the debt was

of Lords, 328; *Webster v. Upton*, 91 U. S. 65 (1875).

¹ This is the case in the California statute, under which mining corporations are created. *Larrabee v. Baldwin*, 35 Cal. 155 (1868); Cal. Statutes, 1853, p. 90, § 16; p. 92, § 27.

² Liability always attaches to those who were such at the time of dissolution or winding up. *Castello's Case*, L. R. 8 Eq. 504 (1869); *Symon's Case*, L. R. 5 Chan. 298 (1870).

³ *Nixon v. Green*, 11 Exch. 550, affirmed 25 L. J. Exch. 209 (1856); *Dodgson v. Scott*, 2 Exch. 457 (1848); *Longley v. Little*, 26 Me. 162 (1846); *Bond v. Appleton*, 8 Mass. 472 (1812); *McClaren v. Franciscus*, 43 Mo. 452 (1869); *Douchy v. Brown*, 24 Vt. 197. *Cf. Deming v. Bull*, 10 Conn. 409 (1835). Under the provision of a charter that stockholders should "at all times be liable for all debts due by said corporation," it was held that those who were members when the debt

was contracted, but had transferred their stock absolutely and in good faith before the commencement of the suit against the corporation, are not to be held liable under the statute. *Middletown Bank v. Magill*, 5 Conn. 28 (1823); *Child v. Coffin*, 17 Mass. 64 (1820); *Curtis v. Harlow*, 12 Metc. 3 (1846); *Southmayd v. Russ*, 3 Conn. 52 (1819).

⁴ *Chesley v. Pierce*, 32 N. H. 388 (1855); *Castleman v. Holmes*, 4 J. J. Marsh. 1 (1839); *Mill Dam Foundry v. Hovey*, 21 Pick. 417 (1839); *Holyoke Bank v. Burnham*, 11 Cush. 183 (1853); *Southmayd v. Russ*, 3 Conn. 52 (1819); *Williams v. Hanna*, 40 Ind. 535 (1872); *Larrabee v. Baldwin*, 35 Cal. 155 (1868); *Mokelumne Hill Canal, &c., Co. v. Woodbury*, 14 Id. 265 (1859); *Moss v. Oakley*, 2 Hill, 265 (1842); *Judson v. Rossie Galena Co.*, 9 Paige, 598 (1842); *McCullough v. Moss*, 5 Denio, 567 (1846). *Cf. Roosevelt v. Brown*, 11 N. Y. 148 (1854); *Cutting v. Damerel*, 68 Id. 410 (1882).

contracted.¹ In New York, by statute, shareholders in manufacturing corporations, who have transferred their shares, are liable on debts existing at the time of the transfer only when suit is commenced against them within two years from the date of the transfer.²

§ 261. *Transferrer not liable for debts incurred after the registry.*—It is a well settled rule of law that a transferrer of stock cannot be charged with corporate indebtedness incurred after the transfer has been regularly made and duly recorded in the corporate books.³ This rule follows as a matter of course, from the

¹ *Moss v. Oakley*, 2 Hill, 265 (1842); *Judson v. Rossie Galena Co.*, 9 Paige, 598 (1842); *McCullough v. Moss*, 5 Denio, 567 (1846); *Tracy v. Yates*, 18 Barb. 152 (1854); *Adderly v. Storm*, 6 Hill, 624 (1844); *Freeland v. McCullough*, 1 Denio, 414 (1845); *Harger v. McCullough*, 2 Id. 119 (1846); *Mokelumne Hill Canal Co. v. Woodbury*, 14 Cal. 265 (1859); *Davidson v. Rankin*, 34 Id. 503 (1868); *Larrabee v. Baldwin*, 35 Id. 155 (1868); *Williams v. Hanna*, 40 Ind. 535 (1872). *Acc. Brown v. Hitchcock*, 36 Ohio St. 667 (1881). It is not always clear precisely when a given indebtedness may be held to have been "contracted." When a corporate note has been renewed it is doubtful whether the renewal operates to create a new indebtedness, or to continue and perpetuate that indebtedness for which the original note was given. In Ohio it is held that a renewal which is a payment or extinguishment of the debt, discharges the shareholders who were bound under the old note. *Wheeler v. Faurot*, 37 Ohio St. 26 (1881). And in Maine the date of the second or renewed note is taken as the time when the indebtedness accrued. *Milliken v. Whitehouse*, 49 Me. 527 (1860). While in Massachusetts the debt is said to be contracted when the corporation accepts a bill of exchange. *Byers v. Franklin Coal Co.*, 106 Mass. 131 (1870). *Cf. Freeland v. McCullough*, 1 Denio, 414, 426 (1845). It has been held that the debt does not accrue, as against the shareholder, at the time judgment thereon is recovered against the corporation. *Larrabee v. Baldwin*, 35 Cal. 155, 168 (1868). In this case *Sawyer, C. J.*, said: "The claim of the respondent, that the judgment is itself a contract creating a new debt, within the

meaning of the statute, for which all who were stockholders at the date of the rendition of the judgment are personally liable, is too absurd to require argument to refute it. That a judgment is a contract of record, in a certain legal sense, may be conceded, but it creates no such new liability as the statute in question contemplates. The judgment only merges and puts in a new form, against the will of both corporation and stockholders, an indebtedness which has already been contracted. If this is to be construed as the creation of a new liability, there would be no way for a stockholder to escape personal liability for all debts which had before been incurred, and the limitation provided for by section 16 of the act concerning corporations for mining companies would be utterly nugatory." As to when a debt may be deemed to have been contracted for the purpose of the action against shareholders, see, in addition to the cases in the preceding notes, *Castleman v. Holmes*, 4 J. J. Marsh. 1 (1839); *Freeland v. McCullough*, 1 Denio, 414, 426 (1845); *Mill Dam Foundry v. Hovey*, 21 Pick. 417 (1839); *Holyoke Bank v. Burnham*, 11 Cush. 183 (1853); *Garrison v. Howe*, 17 N. Y. 458, 464 (1858).

² N. Y. Laws of 1848, ch. 40, § 24.

³ *Chouteau Spring Co. v. Harris*, 20 Mo. 382 (1855); *McClaren v. Franciscus*, 43 Id. 452 (1869); *Miller v. Great Republic Ins. Co.*, 50 Id. 55; *Moss v. Oakley*, 2 Hill, 265 (1842); *Cowles v. Cromwell*, 25 Barb. 413 (1857); *Cole v. Ryan*, 52 Id. 168 (1868); *Johnson v. Underhill*, 52 N. Y. 203 (1873); *Middletown Bank v. Magill*, 5 Conn. 28 (1823); *Johnson v. Laffin*, 5 Dill. 65 (1878); *Grissell v. Bristowe*, L. R. 3 C. P. 112 (1868); *Huddersfield Coal Co. v. Buckley*, 7 Term Rep. 36 (1796); *Croxtan's Case*, 1 De G., M. & G. 600 (1852);

fact that, after registry of a transfer, not only has the transferrer ceased to have an interest in the corporation, but by the registry he has given notice to all future creditors of the corporation that they cannot look to him as security for their debts.

§ 262. *Transferrer can claim exemption from liability for corporate indebtedness by reason of the transfer only after a registry of the transfer.*—The transferrer of stock is not released by the transfer from any statutory liability existing at the time of the transfer, and up to the time of a due and regular registry of the same.¹ This rule is based in justice and a proper regard for the rights of corporate creditors. They have a right to presume that the registered stockholders are the real stockholders, and to hold them liable as such. Until a registry is obtained, the transferrer allows himself to appear, on the corporate books, as a stockholder in the corporation, and corporate creditors are protected in contracting with the corporation on that appearance. Hence, where an owner of shares transfers them in the usual way, by an endorsement of the certificate, with power of attorney to the transferee to have them transferred to the latter upon the corporate records, but the transfer is not so recorded, the transferrer continues to be liable to corporate creditors as though no transfer had been attempted. Until the transfer is duly recorded, it is ineffectual to discharge the transferrer from liability to corporate creditors. As to them, it will be deemed to have been made only at the date of the record thereof in the corporate stock book.² Such also is the rule of the English

Mayhew's Case, 5 Id. 837 (1854); Sutton's Case, 3 De G. & Sm. 262 (1850). See Nixon v. Green, 11 Exch. 530; s. c. aff'd, 25 L. J. Exch. 209 (1856). Cf. Bond v. Appleton, 8 Mass. 472 (1812); Marcy v. Clark, 17 Id. 330 (1821); Curtis v. Harlow, 12 Metc. 3 (1846); Williams v. Hanna, 40 Ind. 535 (1872); Hager v. Cleveland, 36 Md. 476 (1872); Holyoke Bank v. Burnham, 11 Cush. 183 (1853), under peculiar statutes.

¹ Wheeler v. Faurot, 37 Ohio St. 26 (1881); Brown v. Hitchcock, 36 Id. 667 (1881); Wehrman v. Reakirt, 1 Cinn. Super. Ct. 230 (1871). Cf. Jackson v. Sligo Manfg., &c., Co., 1 Lea (Tenn.), 210 (1878). In an action to charge a transferrer for corporate debts incurred between transfer and registry, the transferee is, in Ohio, a necessary party. Wheeler v. Faurot, 37 Ohio St. 26 (1881).

² Shellington v. Howland, 53 N. Y. 371 (1873); Johnson v. Underhill, 52 Id. 203 (1873); Veiller v. Brown, 18 Hun, 571 (1879); Richardson v. Abendroth, 43 Barb. 162 (1864); Worrall v. Judson, 5 Id. 210 (1849); Matter of The Empire Bank, 18 N. Y. 200 (1858); Adderly v. Storm, 6 Hill, 624 (1844); Dane v. Young, 61 Me. 160 (1872); Skowegan Bank v. Cutler, 49 Id. 315 (1860); Fowler v. Ludwig, 34 Id. 455 (1852); Stanley v. Stanley, 26 Id. 191 (1846); Wehrman v. Reakirt, 1 Cinn. Super. Ct. 230 (1871); State v. Ferris, 42 Conn. 560 (1875); Johnson v. Laffin, 5 Dill. 65 (1878); Crease v. Babcock, 10 Metc. 525 (1846); Grew v. Breed, 10 Id. 569 (1846); Holyoke Bank v. Burnham, 11 Cush. 183 (1853); Irons v. Manufacturers' Natl. Bk., 27 Fed. Rep. 591 (1886); Price v. Whitney, 28 Fed. Rep. 297 (1886).

courts.¹ The corporate creditor need not show that, in determining who were shareholders, he relied on the corporate stock book.²

Where, however, the corporation accepts the transferee as a stockholder, and treats him as such, the corporation is estopped to deny that he is such, and cannot hold the transferrer liable for calls, even though no registry of the transfer has been made.³ There is also to be found, a line of cases holding that when the transferrer has done all in his power to complete the transfer, and is guilty of no laches, his liability to corporate creditors is thereby determined, and that accordingly he is discharged as though the registry had been made.⁴

¹ *Marino's Case*, L. R. 2 Chan. 596 (1867); *Musgrave & Hart's Case*, L. R. 5 Eq. 193 (1867); *Walker's Case*, L. R. 6 Eq. 30 (1868); *McEuen v. West London Wharves, &c., Co.*, L. R. 6 Chan. 655 (1871); *Gower's Case*, L. R. 6 Eq. 77 (1868); *Price & Brown's Case*, 3 De G. & Sm. 146 (1850); *Humby's Case*, 5 Jur. (N. S.) 215 (1859); *Barrett's Case*, 4 De G., J. & S. 416 (1864); *Head's Case*, L. R. 3 Eq. 84 (1866); *White's Case*, L. R. 3 Eq. 86 (1866); *Shepherd's Case*, L. R. 2 Chan. 16 (1866); *Straffon's Executor's Case*, 1 De G., M. & G., 576 (1852).

² *Magruder v. Colston*, 44 Md. 349, 356 (1875). *Of. Fisher v. Seligman*, 75 Mo. 13 (1881); *Adderly v. Storm*, 6 Hill, 624 (1844); *Crease v. Babcock*, 10 Metc. 525 (1846); *Matter of The Empire City Bank*, 18 N. Y. 200, 224 (1858); *Holyoke Bank v. Burnham*, 11 Cush. 183, 187 (1853).

³ *Isham v. Buckingham*, 49 N. Y. 216 (1872); *Cutting v. Damerel*, 88 Id. 410 (1882); *Strange v. H. & T. C. R. R. Co.*, 53 Texas, 162 (1880); *Upton v. Burnham*, 3 Biss. 431, 520 (1873). The shareholder cannot set up for defense to an action by a corporate creditor, that some third person had contracted to purchase his shares, or a portion of them, but that with the consent of the corporate authorities, it had been agreed that, until that third person had paid the notes given for the purchase price of the stock, the transfer should not be made on the corporate stock-book. *Phoenix Warehousing Co. v. Badger*, 67 N. Y. 294 (1876); affirming s. c. 6 Hun, 293 (1875). Nor is it a defense for the transferrer, that he had attempted in good faith to have the transfer recorded. He is, in general, discharged only when the transfer is actually

recorded, and duly recorded in the stock-book, and when all the prescribed conditions of a valid transfer have been duly complied with. *McEuen v. West London Wharves, &c., Co.*, L. R., 6 Chan. 655 (1871); *Midland, &c., Ry. Co. v. Gordon*, 16 Mee. & W. 804 (1847); *Sayles v. Blane*, 19 L. J. (Q. B.) 19 (1849); *Ex parte Hall*, 5 Railway & Canal Cases, 624 (1849); *Cartmell's Case*, L. R., 9 Chan. 691 (1874); *Heritage's Case*, L. R., 9 Eq. 5 (1869); *Hennessy's Executor's Case*, 3 De G. & Sm. 191 (1850); *Ex parte Henderson*, 19 Beav. 107 (1854). See also *Bank v. Lanier*, 11 Wall. 369 (1870); *Johnson v. Laffin*, 5 Dill. 65, and the note, page 86 (1878). But see also *contra*, *Bargate v. Shortridge*, 5 H. L. Cas. 297; *Evans v. Smallcombe*, L. R., 3 House of Lords, 249 (1868). That the failure to record the transfer is the fault of the corporation itself, or of the officer thereof whose duty it is to make the entries in the stock-book, is not sufficient to relieve the shareholder who, having transferred his shares, fails to see to it that the proper entry is actually and duly made. *In re Bachman*, 12 Nat. Bank. Reg. 223 (1875). *Of. Ex parte Henderson*, 19 Beav. 107 (1854).

⁴ *Fyfe's Case*, L. R., 4 Chan. 768 (1869); s. c. L. R., 9 Eq. 589 (1870); *Nation's Case*, L. R., 3 Eq. 77 (1866); *Hill's Case*, L. R. 4 Chan. 769 (note) (1869); *Ward & Garfit's Case*, L. R., 4 Eq. 189 (1867); *Ward's Case*, L. R., 2 Eq. 226 (1866); *Ex parte Henderson*, 19 Beav. 107 (1854); *Shortridge v. Bosanquet*, 16 Beav. 84 (1852); overruling s. c. *sub nom.* *Bosanquet v. Shortridge*, 4 Exch. 699 (1850). In *White's Case*, L. R., 3 Eq. 86 (1866), a transferrer was held not discharged because of laches.

§ 263. *The transferee's statutory liability.*—The transferee of stock who has been accepted by the corporation as a shareholder, and whose name has been duly entered on the stock-book as a shareholder, becomes thereupon liable on the stock to corporate creditors whose debts were contracted by the corporation subsequently to the registry of the transfer. As the discharge of the transferor dates from the formal record of the transfer, so the chargeability of the transferee arises out of the same formality. The registry which operates to release the transferor, at the same time operates to charge the transferee.¹ It is not material, that no certificate had been issued to the transferee, or that the corporation had not issued certificates to any of the shareholders.² Nor will the transferee be heard to allege as defense against an action to enforce the statutory liability, that he was induced by fraudulent representations to purchase the shares.³ But the statutory liability does not attach to a shareholder, in respect of debts contracted before he became a member of the corporation.⁴ It has been held, also, that a purchaser of stock may be held liable to creditors, upon the liability imposed by statute, although the transfer is not recorded.⁵

¹ Webster v. Upton, 91 U. S. 65 (1875); Chubb v. Upton, 95 Id. 665 (1877); De Pass's Case, 4 De G. & J. 544 (1859); Cape's Executor's Case, 2 De G., M. & G. 562 (1852); Mann v. Currie, 2 Barb. 294 (1848); Chesley v. Pierce, 32 N. H. 388 (1855).

² Mitchell v. Beckman, 64 Cal. 117; s. c. 16 Rep. 586; Agricultural Bank v. Wilson, 24 Me. 273 (1844).

³ Oakes v. Turquand, L. R., 2 House of Lords, 325 (1867); Houldsworth v. City of Glasgow Bank, L. R., 5 App. Cas. 317 (1880); Tennent v. City of Glasgow Bank, L. R., 4 App. Cas. 615 (1879), and see Chapter IX. Cf. Slater's Case, 35 Beav. 391 (1866).

⁴ Tracy v. Yates, 18 Barb. 152 (1854).

⁵ Laing v. Burley, 101 Ill. 591 (1882); Brown v. Hitchcock, 36 Ohio St. 667 (1881); *In re South Mountain, &c.*, Mining Co., 7 Sawyer, 30 (1881). Where a certificate of stock was issued to one by a wrong christian name by mistake, in an action to enforce his liability as a stockholder, the creditor may introduce parol evidence to show the mistake. Cleveland v. Burnham, 55 Wis. 598 (1885). The court will determine the liability as between the transferor and transferee, in

connection with the corporate creditor's suit, brought to enforce that liability. Mason v. Alexander, 13 Am. & Eng. Corp. Cases, 54 (Ohio, 1886). Transferees of stock in New York manufacturing corporations, are liable under the Laws of 1848, ch. 40, § 24, which is as follows:

"No stockholder shall be personally liable for the payment of any debt contracted by any company formed under this act, which is not to be paid within one year from the time the debt is contracted, nor unless a suit for the collection of such debt shall be brought against such company within one year after the debt shall become due; and no suit shall be brought against any stockholder who shall cease to be a stockholder in any such company, for any debt so contracted, unless the same shall be commenced within two years from the time he shall have ceased to be a stockholder in such company, nor until an execution against the company shall have been returned unsatisfied in whole or in part." See Hastings v. Drew, 76 N. Y. 9 (1879); Shellington v. Howland, 53 N. Y. 371; Handy v. Draper, 89 N. Y. 334 (1882); Freeland v. McCullough, 1 Denio, 414, 426; Veiler v. Brown, 18 Hun, 571; Fisher v. Marvin, 47 Barb. 159

§ 264. *Liability of transferee to transferor by way of indemnity.*—In every contract for the sale of stock, there is an implied undertaking, in the absence of an express provision to the contrary, upon the part of the purchaser, to assume and be responsible for all subsequent liability attaching to the stock. It, however, frequently happens, generally because of a failure to register the transfer, that the vendor or transferor of the stock is obliged to pay a charge upon the stock which accrued after the sale was made. In such a case, it is the well established rule that the transferor may have indemnity, to the full extent of what he is compelled to pay, from the purchaser and transferee of the shares.¹

§ 265. *A transfer to an insolvent to escape liability.*—In the United States a transfer of shares in a failing concern, made by the transferor, with the intention and for the purpose of escaping liability as a shareholder, to a person who for any cause is incapable of responding in respect of such liability, is void, both as to creditors of the company and as to other shareholders, and that,

(1866). Under the Mass. Mfg. Act, "the liability extends to all persons who were stockholders when the debt sought to be enforced was contracted, and also to all persons who are stockholders when the liability is sought to be enforced, although they may have become such since the debt was contracted, but it does not extend to persons who had become stockholders after the debt was contracted, and had ceased to be such before the debt became payable and action was brought." *Sales v. Bates*, 2 N. E. Rep. 633 (R. I. 1886).

¹ *Johnson v. Underhill*, 52 N. Y. 203 (1873); *Hutzler v. Lord* (Maryland, 1886), 4 East. Rep. 809; *Kellogg v. Stockwell*, 75 Ill. 68; *Castellan v. Hobson*, L. R., 10 Eq. 47 (1870); *Wynne v. Price*, 3 De G. & Sm. 810 (1849); *Walker v. Bartlett*, 36 Eng. Law & Eq. 368 (1856); *Grissell v. Bristowe*, L. R., 3 C. P. 112 (1868); *Evans v. Wood*, L. R., 5 Eq. 9 (1867); *Kellock v. Enthoven*, L. R., 9 Q. B. 241 (1873); *Bowring v. Shepherd*, L. R., 6 Q. B. 309 (1871); *Hawkins v. Maltby*, L. R., 6 Eq. 505 (1868); *Allen v. Graves*, L. R., 3 Q. B. 478 (1870); *Shaw v. Rowley*, 16 Mee. & W. 810 (1847). Cf. *Sayles v. Blayne*, 14 Q. B. 205 (1849); *Coles v. Bristowe*, L. R., 4 Chan. 3 (1868); *Humble v. Langs-*

ton, 7 Mee. & W. 517 (1841). "A vendor of shares," says Morawetz, "may, by bill in equity, compel the purchaser to do all things necessary to be done on his part to obtain a complete transfer of the shares, and to indemnify the vendor on account of his liability to the corporation and its creditors." Morawetz on Corporations (2d edition), § 175. Such a suit is said to be in the nature of a suit to enforce specific performance. *Paine v. Hutchinson*, L. R., 3 Eq. 257 (1866); *Shaw v. Fisher*, 2 De G. & Sm. 11 (1848); s. c. 5 De G., M. & G. 596 (1855); *Cheale v. Kenward*, 3 De G. & J. 27. In Ohio, under the act creating statutory liability on the part of shareowners, transferees are liable, as between themselves and their vendors, for all indebtedness of the corporation, whether incurred before or after the transfer, "as if they had owned the stock from the organization of the company." *Wheeler v. Faurot*, 37 Ohio St. 26 (1881); *Brown v. Hitchcock*, 36 Id. 667 (1881), a case wherein the question of statutory liability is very fully and satisfactorily discussed. See also *Cape's Case*, 2 De G., M. & G. 562 (1852). That a transferor may compel the transferee to register the transfer see Ch. XXII.

too, although, as between the transferrer and transferee, the transaction may have been absolute and no secret trust involved.¹ But, on the other hand, if the transfer is *bona fide*, and the transferrer is ignorant of the insolvency of the transferee, the transfer is valid, and the transferrer is released from liability.² The creditor's remedy to enforce the liability of a shareholder who has in this way fraudulently assigned or transferred his stock, is in a Court of Chancery.³

§ 266. *The rule in England.*—The rule in England is that a shareholder may transfer his shares, when the company is in a failing condition, to a man of straw for a nominal consideration, and that although the sole purpose of such a transfer be to escape liability, if it be out and out, and not merely colorable and col-

¹ Nathan v. Whitlock, 3 Edw. Chan. (N. Y.) 215 (1838); s. c. 9 Paige, 152 (1841); Veiller v. Brown, 18 Hun, 571 (1879), by Daniels, J., a well-considered case. McLaren v. Franciscus, 43 Mo. 452 (1869); Miller v. Great Republic Ins. Co., 50 Id. 55 (1872); Provident Savings Institution v. Jackson Place Skating and Bathing Rink, 52 Id. 557 (1873); Chouteau Spring Co. v. Harris, 20 Id. 382; Mandion v. Fireman's Ins. Co., 11 Rob. (La.) 177 (1845); *In re* Bachman, 12 Nat. Bank. Reg. 223 (1875); Marcy v. Clark, 17 Mass. 330 (1821); Central Agricultural, &c., Association v. Alabama Gold Life, &c., Co., 70 Ala. 120 (1881); Gaff v. Fleisher, 33 Ohio St. 107 (1877); Union Mutual Ins. Co. v. Frear Stone Manufg. Co., 97 Ill. 537, 549 (1881); Douchy v. Brown, 24 Vt. 197; Aultman's Appeal, 98 Penn. St. 505 (1881); Everhart v. West Chester, &c., R. R. Co., 28 Id. 339 (1857); Rider v. Morrison, 54 Md. 429 (1880); Paine v. Stewart, 33 Conn. 516 (1866); Roman v. Fry, 5 J. J. Marsh. 634 (1831); Bowden v. Santos, 1 Hughes (U. S.), 158 (1877); Johnson v. Laffin, 5 Dill. 65 (1878); s. c. 6 Central Law Jour., 124; Wehrman v. Reakirt, 1 Cin. Super. Ct. 230 (1871); National Bank v. Case, 99 U. S. 628, 632 (1878); Bowden v. Johnson, 107 Id. 251 (1882); Davis v. Stevens, 17 Blatchf. 259 (1879). Cf. Sawyer v. Hoag, 17 Wall. 610 (1873); Johnson v. Southwestern Railroad Bank, 3 Strobb. Eq. (S. C.) 263 (1848); Allen v. Montgomery R. R. Co., 11 Ala. 457 (1847); Melvin v. Lamar Ins. Co., 80 Ill. 446 (1875); Zirkel v. Joliet Opera House Co., 79 Id. 334 (1875); Adderly v. Storm, 6

Hill, 624, 628 (1844); Billings v. Robinson, 28 Hun, 122 (1882); aff'd, 94 N. Y. 415 (1884).

It is also held that the owner of stock cannot escape liability by transferring it to his infant children, or by taking it originally in their name. Roman v. Fry, 5 J. J. Marsh. 634 (1831). Nor is it any defense to show that the holder took and held the stock as agent of the corporation to sell for its benefit. Allibone v. Hager, 46 Penn. St. 48. It has been held also that no transfer made in anticipation of a judgment against the corporation, and for the purpose of escaping liability, is valid, and shareholders who make such a transfer will be held liable. McLaren v. Franciscus, 43 Mo. 452 (1869); Marcy v. Clark, 17 Mass. 330 (1821).

² Miller v. Great Republic Ins. Co., 50 Mo. 55 (1872). Cf. Billings v. Robinson, 94 N. Y. 415 (1884); s. c. 28 Hun, 122 (1882).

A stockholder who promises a corporate creditor, at a time when the company's affairs are involved, that he will not transfer, thereby inducing him not to sue to collect his debt, is liable to such creditor in case he does transfer. Paine v. Stewart, 33 Conn. 516 (1866). But a transfer will be held valid, it seems, when it is made pursuant to an antecedent option agreement, although the transfer is really made in order to avoid liability. Holyoke Bank v. Burnham, 11 Cush. 183 (1853); Magruder v. Colston, 44 Md. 349 (1875). Cf. Chapman v. Shepherd, L. R. 2 C. P. 228 (1867).

³ Johnson v. Southwestern Railroad Bank, 3 Strobb. Eq. (S. C.) 263 (1848).

lusive with a secret trust attached, it is valid, and the transferrer is thereby released from liability, both as to corporate creditors and the other shareholders.¹ But if the transfer is merely colorable, and there seems to exist a secret trust in favor of the transferrer as to the stock conveyed, or if, in fact, the transferee be merely a nominee of the transferrer, so that as between the parties there has been no *bona fide* transfer, but the object appears to have been to secure the shares to the transferrer in the event that the concern becomes prosperous, but to leave them to the transferee if there is a winding up, the transferrer's name will be put in the list of contributories, and the pretended transfer be wholly set aside.²

The right to transfer shares in England seems to exist up to

¹ De Pass's Case, 4 De G. & J., 544 (1859); Weston's Case, L. R. 4 Chan. 20 (1868); Harrison's Case, L. R. 6 Chan. 286 (1871); Master's Case, L. R. 7 Chan. 292 (1872); Hakim's Case, L. R. 7 Chan. 296, n. (1872); Bishop's Case, Id. (1872); William's Case, L. R. 1 Chan. Div. 576 (1875); King's Case, L. R. 6 Chan. 196 (1871); Chynoweth's Case, L. R. 15 Chan. Div. 13 (1880); Jessopp's Case, 2 De G. & J. 638 (1858); *In re Taurine Co.*, L. R. 25 Chan. Div. 118 (1883); *Moore v. McLaren*, 11 Up. Can. C. P. 534 (1862); *Battles' Case*, 39 L. J. Chan. 391 (1870). *Cf. Bunn's Case*, 2 De G., F. & J. 275 (1860.)

Thus, in De Pass's Case, 4 De G. & J. 544 (1859), the facts were that De Pass, owning two hundred and fifty shares of stock in the Mexican & South American Company, for which he had paid £1,750, upon learning that the concern was involved, handed the certificate to his clerk, without having previously spoken to him of the matter, saying that he might have the stock for a sovereign, which the clerk instantly paid, and at the same time accepted the shares. In about three weeks this clerk sold the shares to another person in the employ of De Pass. Upon the winding up of the company, which was ordered within a few days after the sale by De Pass to his clerk, although it was shown that the shares at the time of that sale were worth considerably more than a sovereign, still, inasmuch as the transaction appeared to have been absolute, although confessedly made to escape possible liability, it was held that the transfer might stand, and that De Pass was

not liable in respect of the shares after the date of the sale to the clerk. So in Master's Case, L. R. 7 Chan. 292 (1872), a transfer of two hundred and eighty shares of stock, on which £15 per share had been paid, for a nominal consideration to an irresponsible son-in-law of the transferrer, the transfer being made only for the purpose of escaping liability upon the shares, was held to discharge the transferrer.

² *Budd's Case*, 3 De G., F. & J. 297 (1861); *Payne's Case*, L. R. 9 Eq. 223 (1869); *Kintrea's Case*, 39 L. J. Chan. 193 (1869); s. c. L. R. 5 Chan. 95; *Chinnock's Case*, Johns. (Eng. Chan.) 714 (1860); *Costello's Case*, 2 De G., F. & J. 302 (1860); *Hyam's Case*, 1 Id. 75 (1859); *Lund's Case*, 27 Beav. 465 (1859); *Ex parte Bennett*, 18 Id. 339 (1853); *Daniell's Case*, 22 Id. 43 (1856); *Eyre's Case*, 31 Id. 177 (1862); *Munt's Case*, 22 Id. 55 (1856); *Slater's Case*, 35 Id. 391 (1866); *Bank of Michigan v. Gray*, 1 Up. Can. Q. B. 422 (1834); *Cox's Case*, 33 L. J. Chan. 145 (1864); *William's Case*, L. R. 9 Eq. 225, n. (1869); *Capper's Case*, L. R. 3 Chan. 458 (1868); *Mann's Case*, Id. 459, n. (1868); *Mitchell's Case*, L. R. 9 Eq. 363 (1870); *Ex parte Hatton*, 31 L. J. Chan. 340 (1862); *Pugh & Sharman's Case*, L. R. 18 Eq. 566 (1872); *Lanckester's Case*, L. R. 6 Chan. 905, n. (1871); *Gilbert's Case*, L. R. 5 Chan. 559 (1870). *Cf. Castellan v. Hobson*, L. R. 10 Eq. 47 (1870); *Maynard v. Eaton*, L. R. 9 Chan. 414 (1874); *Colquhoun v. Courtenay*, 48 L. J. Chan. 338 (1874); *Richardson's Case*, L. R. 19 Eq. 588 (1875).

the time the company is ordered to be wound up and business is suspended.¹ But after that time the right is gone, and it is the duty of the management to refuse to allow a transfer.² The stockholders, under the English rule, may not, it is very clear, collude with the directors to evade the rules governing transfers for the purpose of evading liability.³ Persons to whom shares have been transferred without their knowledge or assent are not estopped, when the knowledge is brought to them, from repudiating and denying the stockholdership.⁴

¹ De Pass's Case, *supra*, and the cases generally in the preceding notes.

² Mitchell's Case, L. R. 4 App. Cas. 548 (1879); Weston's Case, L. R. 4 Chan. 20, 30 (1868); *Ex parte* Parker, L. R. 2 Chan. 685 (1867); Chappell's Case, L. R. 6 Chan. 902 (1871).

In this country directors have in general no power to refuse or prevent transfers, such as inheres in such boards of management in English companies.

³ Eyre's Case, 31 Beav. 177 (1862); Bennett's Case, 5 De G., M. & G., 284 (1854). Nor may a director make use of his position as director to transfer his stock, and thus escape chargeability upon it. Munt's Case, 22 Beav. 55 (1856). Nor will a stockholder be allowed to relieve himself when he learns of the probable insolvency of the concern by inducing the directors to postpone their application for an order to wind up, until he have time to transfer his shares to a pauper or other irresponsible person. *Ex parte* Parker, L. R. 2 Chan. 685 (1867); Gilbert's Case, L. R. 5 Chan. 559 (1870); Allin's Case, 16 Eq. 449 (1873). And a director who transfers shares standing in his name, to a person already holding all the shares any one person is allowed to hold, will not thereby escape liability. *Ex parte* Brown, 19 Beav. 97 (1854). In general, moreover, a transferrer is not exempt from liability by reason of a transfer, unless the transferee has the present capacity to assume the liability. Nickalls v. Merry, L. R. 7 H. L. 530 (1875); Browne

v. Black, L. R. 8 Chan. 939 (1873); Mann's Case, L. R. 3 Chan. 459, n. (1868). Cf. Johnson v. Laffin, 5 Dill. 65, 81 (1878); Case of the Reciprocity Bank, 22 N. Y. 9 (1860). Accordingly, a transfer to an infant for the purpose of escaping liability is futile. Symon's Case, L. R. 5 Chan. 298 (1870); Weston's Case, Id. 614 (1870); Curtis' Case, L. R. 6 Eq. 455 (1868); Castello's Case, L. R. 8 Eq. 504 (1869); Walsh v. The Union Bank, 5 Quebec, L. R. 289 (1879).

⁴ Birch's Case, 2 De G. & J. 10 (1857); Fox's Case, 3 De G., J. & S. 465 (1863); Higg's Case, 2 Hem. & M. 657 (1865); Somerville's Case, L. R. 6 Chan. 266 (1870). Cf. Bullock v. Chapman, 2 De G. & Sm. 211 (1848). And see also case of the Reciprocity Bank, 22 N. Y. 9 (1860). A colorable transfer, as has appeared, will not operate to discharge the transferrer where shares were collusively assigned to a servant for the purpose of evading liability. Hence when the servant, upon the concern becoming solvent, attempted to claim the shares as though the transfer had been out and out, the court, having previously decided against the *bona fides* of the transaction, held the owner entitled to a declaration that the servant held the shares in trust for him. Colquhoun v. Courtenay, 43 L. J. Chan. 338 (1874). As to a transfer made in ignorance of the fact that a winding up has been commenced, see Emmerson's Case, L. R. 1 Ch. 433 (1866).

CHAPTER XVI.

ISSUE OF PREFERRED STOCK AND STOCK UPON WHICH INTEREST IS GUARANTEED.

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| <p>§ 267. What is preferred stock.</p> <p>268. Power to issue preferred or guaranteed stock.</p> <p>269. General rights of preferred stockholders.</p> <p>270. Preferred shareholders are not creditors, and are entitled to dividends only from profits.</p> <p>271. The discretion of directors with respect to declaring dividends on preferred stock.</p> <p>272. Arrears of preferred dividends, to</p> | <p>what extent payable subsequently.</p> <p>§ 273. The option to exchange common for preferred shares.</p> <p>274. Rights of the assignee or transferee of preferred shares in arrears of dividends.</p> <p>275. Special stock in Massachusetts.</p> <p>276. Remedies of shareholders herein.</p> <p>277. Interest-bearing stock.</p> <p>278. Rights of preferred shareowners on dissolution.</p> |
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§ 267. *What is preferred stock.*—By preferred stock is to be understood stock which entitles the holder to receive dividends from the earnings of the company before the common stock can receive a dividend from such earnings,¹ or stock entitled to dividends from the income or earnings of the corporation before any other dividend can be paid.² The relation of debtor and creditor does not exist between the preferred stockholders and the corporation, and the right to a preferred or guaranteed dividend is not a debt until the dividend is declared. A dividend is money paid out of profits by a corporation to its shareholders. A preferred dividend is nothing more than that which is paid to one class of shareholders in priority to that to be paid to another class.³

¹ *Totten v. Tison*, 54 Ga. 139 (1875). Such stock is called indifferently preferred, preference, preferential or guaranteed stock. *Henry v. Great Northern, &c., Ry. Co.*, 4 Kay & J. 1 (1857).

² *Chaffee v. Rutland R. R. Co.*, 55 Vt. 110 (1882).

³ *Belfast, &c., R. R. Co. v. Belfast*, 77 Me. 445 (1885); *Taft v. Hartford, &c., R. R. Co.*, 8 R. I. 310, 333 (1866); *Chaffee v. Rutland, &c., R. R. Co.*, 55 Vt. 110 (1882). In *Burt v. Rattle*, 81 Ohio St. 116 (1876), it was held that the holder of preferred stock was a creditor, but that

was a case where there had been practically a loan on mortgage. The mortgagees were only nominally preferred shareholders and did not have any right to vote at corporate meetings, and were not liable for corporate debts. The prevailing rule, it is believed, is correctly stated in the text. A preferred dividend has also been defined as "substantially interest chargeable exclusively on profits." *Henry v. Great Northern Ry. Co.*, 1 De G. & J. 606, 637; *Crawford v. North Eastern, &c., R. R. Co.*, 3 Jur. (N. S.) 1093 (1856). And preferred shares entitle the holder

In the United States the terms "preferred," and "guaranteed," as applied to stock, are essentially convertible,¹ although in England they distinguish guaranteed stock as stock that is entitled to arrears, and preferred or preference stock as stock not so entitled.² Accordingly in this country a guaranteed or preferred dividend, like a preferred dividend in England, is said to be "a pledge of the funds, legally applicable to the purposes of a dividend."³

§ 268. *Power to issue preferred or guaranteed stock.*—The issue of preferred stock is not usually incidental to the ordinary exercise of corporate functions. It is not the regular and ordinary course of business. On the contrary it is an unusual and extraordinary course to be resorted to only when particular reasons or emergencies render it necessary. The right or power of the corporation to issue such stock has been the subject of much controversy. When it is expressly granted in the charter by which the company is incorporated then, as of course, there is no question as to the legality of the issue.⁴ Sometimes a statute provides for the exchange under prescribed conditions of common for preferred stock.⁵ But it is plainly the law that the corporation, of

to say, "nobody shall have any portion of the profits of the company until I have been paid my dividend." *Henry v. Great Northern Ry. Co.*, 4 Kay & J. 1, 32 (1857).

¹ *Taft v. Hartford, &c., R. R. Co.*, 8 R. I. 310, 333, 334, 335 (1866).

² *Henry v. Great Northern Ry. Co.*, 4 Kay & J. 1, 12, 21 (1857).

³ *Taft v. Hartford, &c., R. R. Co.*, 8 R. I. 310, 335 (1866).

⁴ *Everhart v. West Chester, &c., R. R. Co.*, 28 Penn. St. 339 (1857); *Rutland, &c., R. R. Co. v. Thrall*, 35 Vt. 538, 545 (1863). *Cf. Davis v. Proprietors, &c.*, 49 Mass. 321 (1844); *Williston v. Michigan, &c., R. R. Co.*, 95 Id. 400 (1866). And when such power is given by legislative enactment it is held that a single stockholder cannot prevent an issue thereunder, which is to say that when the legislature confers powers in this respect upon the managers of a corporation, with the assent of the shareholders, no one shareholder, by refusing his assent, can hinder the exercise of the power. *Curry v. Scott*, 54 Penn. St. 270 (1867). Under a power to increase capital stock "in such manner, and with and subject to such rules, regulations, privileges, and condi-

tions," as the company may see fit, it has been held that preferred stock may be issued. *Harrison v. Mexican, &c., R. R. Co.*, L. R. 19 Eq. Cas. 358 (1875).

⁵ *Webb v. Earle*, L. R., 20 Eq. 556 (1875); New York Session Laws, 1880 ch. 225. Under the powers conferred by the statute, 30 & 31 Vict., c. 127, various plans have been devised by English companies on the verge of insolvency to raise funds, and a favorite device is the issue of preferred shares of stock. Thus, for example, that there should be five kinds of preference shares, some with a "preferential dividend" out of working profits, some with "preferential dividends," and others with "a preferential interest or dividend." *Corry v. Londonderry, &c., Ry. Co.*, 29 Beav. 263 (1860). See also, by way of illustration as to these various methods in England of raising funds by the issue of preferred shares, *Matthews v. Great Northern, &c., Ry. Co.*, 28 L. J. Chan. 375 (1859); *Re Cambrian Ry. Co.*, L. R., 3 Chan. 278 (1868); *Re Potteries, &c., Ry. Co.*, Id. 67 (1867); *Webb v. Earle*, L. R., 20 Eq. 556 (1875); *Stevens v. Midland, &c., Ry. Co.*, L. R., 8 Chan. 1064 (1873); *Re Bristol, &c., Ry. Co.*, L. R., 6 Eq. 448 (1868); *Re Devon*,

itself, has no implied power, either at the time of its organization,¹ or at any subsequent time, to issue preferred stock. The power exists only when expressly conferred by the charter or by statute.²

&c., Ry. Co., Id. 610 (1868); *Munas v. Isle of Wight Ry. Co.*, L. R., 8 Eq. 665 (1869); *Re East & West, &c., Ry. Co.*, Id. 87 (1869); *London, &c., Association v. Wrexham, &c., Ry. Co.*, L. R., 18 Eq. 566 (1874); *Re Anglo Danubian, &c., Co.*, L. R., 20 Eq. 339 (1875); *Midland Ry. Co. v. Gordon*, 16 Mee. & W. 804 (1847). In Kansas, in 1873, it was enacted, "That it shall be lawful for any railroad company created by or existing under the laws of this State, from time to time, to purchase and hold stock and bonds, or either, or to guaranty the payment of the principal and interest, or either, of the bonds of any other railroad company or companies, the line of whose railroad, constructed or being constructed, connects with its own." See *Atchison, &c., R. R. Co. v. Fletcher*, Kansas, April, 1886.

¹ *Semble contra*, in *Kent v. Quicksilver Mining Co.*, 78 N. Y. 159, 178 (1879).

² *Hutton v. Scarborough, &c., Co.*, 4 De G., J. & S. 672 (1865); *Sturge v. Eastern, &c., R. R. Co.*, 7 De G., M. & G. 158 (1865). *In re National, &c., Co.*, 4 Drew. 529 (1859); *Guinness v. Land Corporation of Ireland*, 22 L. R. Ch. Div. 349 (1882); *Moss v. Syers*, 11 Week. Rep. 1046 (1868); s. o. 32 L. J. Chan. 711; *Melhado v. Hamilton*, 28 L. T. (N. S.) 578 (1873); s. o. 29 Id. 364; *Taylor v. South, &c., R. R. Co.*, 4 Woods, 575 (1882). *Cf. Kent v. Quicksilver Mining Co.*, 78 N. Y. 159 (1879); *Bates v. Androscoggin, &c., R. R. Co.*, 49 Me. 491 (1860); *Hazlehurst v. Savannah, &c., R. R. Co.*, 43 Ga. 13 (1871); *Fielden v. Lancashire, &c., Ry. Co.*, 2 De G. & Sm. 531 (1848); *The Railway Companies Act*, 1867, 30 & 31 Vict., ch. 127, §§ 6-17. It has, however, been held that where the power to increase the capital stock exists, preferred stock may be issued by a majority vote, the legality of such an issue being based upon the corporate power to borrow money. *City of Covington v. Covington, &c., Co.*, 10 Bush, 69, 76 (1873); *Harrison v. Mexican, &c., R. R. Co.*, 19 L. R. Eq. Cas. 358 (1875). See also *Rutland, &c., R. R. Co. v. Thrall*, 35 Vt. 536 (1863). *Contra*, *Kent v. Quicksilver Mining Co.*, 78 N. Y. 159 (1879). In this case it

is vigorously argued that the issue of this stock cannot derive validity from the power to borrow money. The court say: "The idea of borrowing is not filled out unless there is in the agreement therefore a promise or understanding that what is borrowed will be repaid or returned, the thing itself or something like of equal value, with or without compensation for the use of it in the meantime. . . . The stockholder [meaning the preferred stockholder] had not by the scope of his bargain, nor by the terms of the written evidence of it, any right ever to ask for repayment of the money furnished by him. In short there was not formed thereby the relation of debtor and creditor. The stockholder parted forever with the money furnished, inasmuch as the charter of the company is perpetual, and the company made a perpetual charge upon its net earnings." This is sound reasoning, and perhaps the better view. But under given conditions undoubtedly a loan may take this shape of preferred shares, as where preferred shares are secured by bond and mortgage, the holders being expressly declared not members of the corporation. *Burt v. Rattle*, 31 Ohio St. 116 (1876). Compare *Totten v. Tison*, 54 Ga. 139 (1875), or where there is a provision for the redemption of the shares, *Westchester, &c., R. R. Co. v. Jackson*, 77 Penn. St. 321 (1875). Compare *Richardson v. Vermont, &c., R. R. Co.*, 44 Vt. 612 (1872); *Rutland, &c., R. R. Co. v. Thrall*, 35 Vt. 536 (1863). And in another case the legality of the issue of preferred stock in such a case, is put upon the ground, not of the right to borrow money, but upon the ground of a right to raise funds by a sale of stock. *Chaffee v. Rutland, &c., R. R. Co.*, 55 Vt. 110 (1882). So also where an act of the legislature authorized the issue of bonds by a county "in subscription for preferred stock" of a railroad company, and the act provided that the county "shall receive from the company preferred stock to the amount of the said bonds, which preferred stock shall bear interest at the rate of seven per cent. per annum," it was held that this preferred stock meant capital stock; that a certificate of stock tendered by the company to

Where the power to issue is in the corporation it cannot be exercised by the directors.¹ When, however, the directors have, without authority, issued such stock, the corporation as a corporation, having the power, it may by a subsequent vote ratify the unauthorized act of the directors and thus validate the issue.² And where the corporation has no implied power to authorize the issue of preferred shares, if such stock is issued, it will by lapse of time become legal, as far as the stockholders are concerned, by the mere acquiescence of the stockholders, who are estopped to deny the validity of that of which they have long had knowledge, by which they have been benefited, and of which they have not complained.³ Thus a delay of four years,⁴ or of ten years,⁵ in raising the question of the validity of an issue of preferred stock, advantages having accrued in the meantime to the corporation, and the shareholders, have been held such acquiescence as will bar the right of a stockholder to object. Acceptance of the preferred stock and dividends thereon also bars the right to challenge the legality of the issue.⁶ So also where the matter was on the whole more favorable to the plaintiff than to other shareholders, it was held in Indiana, in a leading case, that the issue could not be questioned.⁷ But a power to issue preferred stock does not include the power to issue partly preferred and partly non-preferred shares.⁸ Neither can a power to issue a certain number of preferred shares be extended to validate the issue of a greater number.⁹ The stockholders' remedy

the county, setting forth that the county was entitled to the stated amount, but by implication declaring it not to be capital stock, was not sufficient, and that the corporation might be compelled by mandamus to issue a certificate in substantial compliance with the terms of the act. *State v. Cheraw, &c., R. R. Co.*, 16 S. C. 524 (1881). So also it has been held that preferred stock may be issued to retire common stock theretofore issued. *Westchester, &c., R. R. Co. v. Jackson*, 77 Penn. St. 321 (1875). In England it has been held that in order that a company may have power to issue preferred stock, it is not indispensable that the power should be stated in the memorandum of association; it is sufficient if it is given by the articles of association according to their true construction. *Harrison v. Mexican Ry. Co.*, 44 L. J. Chan. 403 (1875).

¹ *McLoughlin v. Detroit, &c., R. R. Co.*, 8 Mich. 100 (1860).

² *McLoughlin v. Detroit, &c., R. R. Co.*, *supra*.

³ *Taylor v. South, &c. R. R. Co.*, 4 Woods, 575 (1882); *Hazelhurst v. Savannah, &c. R. R. Co.*, 43 Ga. 13 (1871); *Lockhart v. Van Alstyne*, 31 Mich. 76 (1875).

⁴ *Kent v. Quicksilver Mining Co.*, 78 N. Y. 159 (1879).

⁵ *Taylor v. South, &c. R. R. Co.*, 4 Woods, 575 (1882).

⁶ *Branch v. Jesup*, 106 U. S. 468 (1882).

⁷ *Evansville, &c. R. R. Co. v. City of Evansville*, 15 Ind. 395.

⁸ *Covington, &c. Co. v. Sargent*, 1 Cin. Super. Ct. 354 (1871).

⁹ *Melhado v. Hamilton*, 28 L. T. (N. S.) 578 (1873); s. c. 29 Id. 364.

to restrain the issue of the preferred stock is by a bill in equity,¹ and he need not wait to commence his suit until there are funds to make a dividend.²

§ 269. *General rights of preferred shareholders.*—The rights, speaking generally, and the *status* of the holder of preferred shares, will in every case depend upon the particular provisions to be found in the certificate of stock which he holds as the evidence of his contract, upon the terms of the contract itself, or upon the statute under and by virtue of which the issue was made.³ The real intent and character of the contract is to be sought for and ascertained by reference to the charter and its amendments, the by-laws and resolutions of the shareholders, books of minutes of corporate meetings, annual reports and other records of corporate action.⁴ The theory that preferred share-

¹ Guinness v. Land Corporation of Ireland, 22 L. R. Chan. Div. 349.

² Sturge v. Eastern, &c. Ry. Co., 7 De G., M. & G. 158 (1855). But a subscriber to the common stock, who has given an express or implied consent to the issue of preferred stock, is not released from liability on his subscription by such issue. Rutland, &c. R. R. Co. v. Thrall, 35 Vt. 536 (1863); Hazelhurst v. Savannah, &c. R. R. Co., 43 Ga. 13 (1871); Hoyt v. Quicksilver Mining Co., 17 Hun, 169; Kent v. Id., 78 N. Y. 159 (1879).

³ Elkins v. Camden, &c. R. R. Co., 36 N. J. Eq. 233 (1882); s. c. Id. 5; Baily v. Hannibal, &c. R. R. Co., 1 Dill. 174 (1871); s. c. 17 Wall. 96; St. John v. Erie Ry. Co., 22 Id. 136 (1874); Williston v. Michigan, &c. R. R. Co., 95 Mass. 400 (1866); West Chester, &c. R. R. Co. v. Jackson, 77 Penn. St. 321 (1875); Matthews v. Great Northern, &c. Ry. Co., 28 L. J. Chan. 375 (1859); Belfast, &c. R. R. Co. v. Belfast, 77 Me. 445 (1885).

⁴ Boardman v. Lake Shore, &c. R. R. Co., 84 N. Y. 157 (1881); Gordon v. Richmond, &c. R. R. Co., 78 Va. 501, 510; Stevens v. South, &c. Ry. Co., 9 Hare, 313 (1851); Sturge v. Eastern, &c. Ry. Co., 7 De G., M. & G. 158 (1855); Corry v. Londonderry, &c. Ry. Co., 29 Beav. 263 (1860); Harrison v. Mexican, &c. Ry. Co., L. R. 19 Eq. Cas. 358 (1875); Kent v. Quicksilver Mining Co., 78 N. Y. 159 (1879); Crawford v. Northeastern, &c. Ry. Co., 3 Jur. (N. S.) 1093 (1856); Henry v. Great Northern, &c. Ry. Co., 3

Id. 1117; Matthews v. Id. 5 Id. 284; Belfast, &c. R. R. Co. v. Belfast, 77 Me. 445 (1885). In Belfast, &c. R. R. Co. v. City of Belfast, 77 Me. 445 (1885), a recent and well considered case, where a railway company in issuing preferred shares adopted a by-law to the intent that its net earnings should be divided semi-annually among the shareholders, first paying upon the preferred shares an amount per annum not exceeding six per cent., and then if there was a surplus an equal amount upon the non-preferred shares, and that then any remaining surplus should be divided equally among all the shareholders, it was held that the subscribers to the preferred stock took their shares upon the conditions named in the by-law, as a contract between them and the corporation. Under the by-law in this case the preferred shareholder was held not a creditor, and that his dividend was not guaranteed to him, but only made payable out of net earnings, and that, inasmuch as the by-law implied that the entire net earnings of each year should be paid out in dividends, a deficiency of preferred dividend, in any year, could not be made up in subsequent years. As to what are "net earnings," see Union Pacific R. R. Co. v. U. S., 99 U. S. 402 (1878); Sioux City, &c. R. R. Co. v. U. S., 110 Id. 205 (1883), § 272, and Chapter on Dividends.

In Gordon v. Richmond, &c. R. R. Co., 78 Va. 501 (1884), where a railway company issued preferred stock under the power so to do, conferred by statute (Act of Feb'y 13, 1856, Acts of

holders are similar to mortgagees, or creditors of the corporation is now nowhere maintained, and it seems to be admitted in all the recent cases that preferred shareholders are simply shareholders or stockholders of the corporation.¹ Like other shareholders—that is to say equally with the holders of the common stock, they have the right to vote at corporate meetings and exercise in full all the other rights of a shareholder.² But this is the limit of their right in these respects. They cannot restrain corporate acts any more, nor on any other or higher grounds than the holders of the common stock.³ Their rights, moreover, are subordinate to those of the corporate creditors.⁴ It is said that a holder of preferred stock issued in lieu of bonds is a creditor for certain purposes,⁵ and that when a holder of preferred stock exercises an option to exchange it for the common stock, he

Va., 1855-56, ch. 130, p. 108), and the plan adopted as to dividends, secured somewhat the same distribution of profits as in the case of *Belfast, &c., R. R. Co. v. Belfast*, (*supra*,) it was held that the preferred stock issued under this act was guaranteed capital in the strictest sense, that the dividends thereon, being limited to seven per cent. per annum, were payable out of the gross receipts of the company, if need be, to the exclusion of the holders of the common stock from any participation in profits; that as to any excess of dividends, beyond seven per cent., the guaranteed and common stock stood upon the same footing, and that, inasmuch as earnings belong primarily to the corporation, and there can be no such thing as a dividend until it is declared, where the directors have failed to declare dividends at the times prescribed in the charter, it is not in their power to declare a dividend to extend back over the periods during which no dividends were paid. See also *Ragland v. Broadnax*, 29 Gratt. 512; *Mills v. North, &c. Ry. Co.*, L. R. 5 Chan. App. 621 (1870). After the preferred stock has been issued it is beyond the power of the corporation to limit the preference given to it. *Ashbury v. Watson*, L. R. 30 Ch. D. 376 (1885).

¹ *State v. Cheraw, &c. R. R. Co.*, 16 S. C. 524 (1881). By so eminent an authority as Mr. Pierce, it is said: "The issue of preferred stock is a mode by which a corporation obtains funds for its enterprises *without borrowing money—or contracting a debt*. Its holders are a

privileged class who are entitled to dividends of a certain per cent., payable out of the net earnings in priority to any dividends upon ordinary stock." (*Pierce on Railways*, 124. See also *Crawford v. Northeastern, &c., Ry. Co.*, 3 Jur. (N. S.) 1093 (1856); *Henry v. Great Northern, &c. Ry. Co.*, 3 Id. 1117. *Emerson v. N. Y. & N. E. R. R. Co.*, 16 R. I. 555 (1884), said, however, the preferred stockholder had rights "against the company and its property which partook of those of a stockholder and of a creditor. As a stockholder he had rights to a dividend and to repayment of the principal of his stock in preference to any of the ordinary stockholders. As a creditor he was entitled to be paid the amount of his debt in the same manner as other creditors, but with no preference over them."

² *Rutland, &c. R. R. Co. v. Thrall*, 35 Vt. 536; *Burt v. Rattle*, 31 Ohio St. 116; *St. John v. Erie Ry. Co.*, 22 Wall. 136.

³ *Warren v. King*, 108 U. S. 389 (1882); *Thompson v. Erie Ry. Co.*, 45 N. Y. 468 (1871); s. c. 11 Abb. Prac. (N. S.) 188; 42 How. Prac. 68; *Garrett v. May*, 19 Md. 177 (1862).

⁴ *St. John v. Erie Ry. Co.*, 22 Wall. 136 (1872); *Warren v. King*, 108 U. S. 389 (1882).

⁵ *St. John v. Erie Ry. Co.*, 22 Wall. 126 (1872); *Rutland, &c. R. R. Co. v. Thrall*, 35 Vt. 536 (1863); *West Chester, &c. R. R. Co. v. Jackson*, 77 Penn. St. 321 (1875); *Phillips v. Eastern R. R. Co.*, 138 Mass. 122 (1884); *Bates v. Androscoggin, &c. R. R. Co.*, 49 Me. 491 (1860).

ceases to be a creditor.¹ But this is a questionable position, and it is plainly not the rule until he exercises the option.²

§ 270. *Preferred shareholders are not creditors and are entitled to dividends only from profits.*—In the earlier decisions there was a tendency to hold that owners of preferred or guaranteed stock are creditors of the corporation, and so entitled to the rights and preferences of creditors in respect to their dividends. But it is now conclusively settled that a shareholder is not a creditor.³ If he were a creditor of the corporation then, like any other creditor, he would be entitled to demand and collect from the corporation the sum specified in his contract, and that without reference to whether the corporation was earning or losing money. Since, however, the preferred shareholder is but a shareholder with a right to have his dividend paid before dividends on the common stock are paid, he is not entitled to any dividend until the corporation has funds which are properly applicable to the payment of dividends, that is to say, until the corporation has earned the money to pay the dividends.⁴ A contract that dividends shall be paid on the preferred stock, whether any profits are made or not, would be contrary to public policy and void.⁵

An agreement to pay dividends absolutely and at all events, that is to say, from the profits when there are any, and from the capital when there are not, is an undertaking which is contrary to law, and is void. Public policy condemns with emphasis any such under-

¹ *Burt v. Rattle*, 31 Ohio St. 116 (1876).

² *Totten v. Tison*, 54 Ga. 139 (1875).

³ *Totten v. Tison*, 54 Ga. 139 (1875); *Belfast, &c., R. R. Co. v. Belfast*, 77 Me. 445 (1885); *Taft v. Hartford, &c., R. R. Co.*, 8 R. I. 310 (1866); *Chaffee v. Rutland, &c., R. R. Co.* 55 Vt. 110 (1882); *Warren v. King*, 108 U. S. 389 (1882).

⁴ *Bates v. Androscoggin, &c., R. R. Co.*, 49 Me. 491 (1860); *Taft v. Hartford, &c., R. R. Co.*, 8 R. I. 310 (1866); *Lockhart v. Van Alstyne*, 31 Mich. 76 (1875); *Chaffee v. Rutland, &c., R. R. Co.*, 55 Vt. 110 (1882); *McGregor v. Home Ins. Co.*, 33 N. J. Eq. 181 (1880); *Warren v. King*, 108 U. S. 389 (1882); *McDougall v. Jersey, &c., Co.*, 2 Hem. & M. 528 (1864). See also *Pittsburg, &c., R. R. Co. v. County of Allegheny*, 63 Penn. St. 126 (1869). The preferred shareowner is, moreover, like other shareholders, liable

for the debts of the corporation. *Burt v. Rattle*, 31 Ohio St. 116 (1876).

⁵ *Lockhart v. Van Alstyne*, 31 Mich. 76 (1875). A dividend means something to be divided, a fund which the corporation sets aside from its profits to be divided among its members. A right to a dividend is not a debt until the dividend is regularly declared. If a dividend is declared to the preferred shareholders exclusively, it must be understood to imply that the sum divided has been realized as profits, but that the earnings do not warrant a dividend on the common stock. A dividend depends essentially upon the good judgment, integrity, and fidelity of the corporate managers—and a guarantee of a dividend is nothing more than an undertaking on the part of the corporation to earn and pay one—to do whatever good judgment, fidelity, and honesty can accomplish to pay such dividend.

taking on the part of a corporation as to its preferred or guaranteed shares.¹ The rule is well settled that dividends on preferred stock are payable only out of the *bona fide* earnings of the company.²

§ 271. *The discretion of directors with respect to declaring dividends on preferred stock.*—In general it is within the discretion of the directors to declare, or not to declare, dividends on the common stock, but with respect to dividends on the preferred stock it is otherwise. The question of the ability of the corporation to pay a preferred dividend is one that may be brought before a court of equity, and the decision of the directors is not conclusive but will be reviewed by the court.³ Where the right to the preferred dividend is clear, and there are funds from which it can properly be made, a court of equity will compel the company to declare it.⁴ But preferred shareholders are not entitled to a dividend which would work an injustice to creditors and the other stockholders, by taking all the money from the treasury and thereby crippling or wrecking the enterprise.⁵ Moreover, it

¹ Lockhart v. Van Alstyne, by Cooley, J., *supra*. See also Curran v. Arkansas, 15 How. 304 (1853); Evansville, &c., R. R. Co. v. City of Evansville, 15 Ind. 395.

² Thompson v. Erie Ry. Co., 45 N. Y. 465 (1871); Boardman v. Lake Shore, &c., R. R. Co., 84 Id. 157 (1881); Prouty v. Id., 52 Id. 363 (1873); Union Pacific R. R. Co. v. U. S., 99 U. S. 402 (1878); Nichols v. New York, &c., R. R. Co., 15 Fed. Rep. 575 (1883); Elkins v. Camden, &c., R. R. Co., 36 N. J. Eq. 233 (1882); Belfast, &c., R. R. Co. v. Belfast, 77 Me. 445 (1885), and the cases *supra*. When two corporations are consolidated, one of which has issued preferred shares, the new company is liable to pay the guaranteed dividends thereon. Prouty v. Lake Shore, &c., R. R. Co., 52 N. Y. 563 (1873); Chase v. Vanderbilt, 62 Id. 307 (1875). In the case, however, of Cotting v. New York & N. E. R. R. Co. 5 New Eng. Rep. 851 (Conn. 1886), the court held that under the peculiar wording of the statute creating preferred stock, the dividend must be paid, although there was a large deficit in the corporate transactions for the year. The court says: "Ordinary preferred stock payable from the surplus, or net profits, takes its chances with common stock; and if, from any cause, a dividend fails, it is gone. But here the agreed

dividend, however long payment may be deferred, keeps its place as a lien upon the net earnings and must be paid in full before any payment can be made to the holders of the common stock. In this respect the preferred dividends closely resemble the interest on bonds."

³ Bailey v. Railroad Co., 17 Wall. 96 (1872); St. John v. Erie Ry. Co., 22 Id. 136 (1874); Barnard v. Vermont, &c., R. R. Co., 89 Mass. 512 (1863); Bryant v. Ohio College, 1 Cinn. 67 (1870); Chase v. Vanderbilt, 37 N. Y. Super. Ct. 334 (1874); Bates v. Androscoggin, &c., R. R. Co., 49 Me. 491 (1860); Dickinson v. R. R. Co., 7 West Va. 390 (1874); Rutland, &c., R. R. Co. v. Thrall, 35 Vt. 536 (1863); Richardson v. Vermont, &c., R. R. Co., 44 Id. 613 (1872); Davis v. Proprietor, &c., 49 Mass. 321 (1844); Williston v. Michigan, &c., R. R. Co., 95 Id. 400 (1866); King v. Ohio, &c., R. R. Co., 9 Rep. 431; Taft v. Hartford, &c., R. R. Co., 8 R. I. 310 (1866); Thompson v. Erie Ry. Co., 45 N. Y. 463 (1871); Prouty v. Lake Shore, &c., R. R. Co., 52 Id. 563 (1873); West Chester, &c., R. R. Co. v. Jackson, 77 Penn. St. 321 (1875); Belfast, &c., R. R. Co. v. Belfast, 77 Me. 445 (1885).

⁴ The cases *supra*.

⁵ Culver v. Reno, &c., Co., 91 Penn. St. 367 (1879).

has been held that earnings ought to be appropriated to the payment of a floating debt in preference to the payment of dividends on the preferred stock.¹ The directors, under an authority to issue preferred stock, have no right to issue it for the purpose of paying dividends therewith upon the common stock.² The authority to issue such stock is usually sought by companies who have expended their original capital, in order to raise additional capital. The issue of the preferred stock increases the capital stock, and since the capital stock can never legally be divided among stockholders, except upon dissolution, the proceeds of an issue of preferred stock is to be added to the permanent funds of the corporation.³

§ 272. *Arrears of preferred dividends, to what extent payable subsequently.*—Preferred stock is stock with a guarantee that the dividends thereon will be paid. Accordingly where there are no net profits, and consequently no funds for a dividend, the contract of guarantee is broken. As soon, however, as there are net profits available for dividends the corporation must pay the preferred dividends and all arrearages thereon, before a dividend is declared on the common stock. This is the well settled rule in this country,⁴ and at common law also, in England.⁵

¹ Chaffee v. Rutland, &c., R. R. Co., 55 Vt. 110 (1882); National Bank v. Douglass, 1 McCrary, 86 (1877); Railroad Co. v. Howard, 7 Wall. 392 (1868); Jones on Railroad Securities, § 620; *In re* London Rubber Co., L. R. 5 Eq. Cas. 525 (1867).

² Hoole v. Great Western Ry. Co., L. R. 3 Chan. 262 (1867).

³ Hoole v. Great Western Ry. Co., L. R. 3 Chan. 262 (1867); Lockhart v. Van Alstyne, 31 Mich. 76 (1875).

⁴ Boardman v. Lake Shore, &c., R. R. Co., 84 N. Y. 157 (1881); Prouty v. Michigan, &c., R. R. Co., 1 Hun, 655 (1873); Elkins v. Camden, &c., R. R. Co., 36 N. J. Eq. 233 (1882); Taft v. Hartford, &c., R. R. Co., 8 R. I. 310 (1866); Lockhart v. Van Alstyne, 31 Mich. 76 (1875). *Contra*, Belfast, &c., R. R. Co. v. Belfast, 77 Me. 445.

⁵ Henry v. Great Northern, &c., Ry. Co., 1 De G. & J. 606; Crawford v. North-eastern Ry. Co., 3 Jur. (N. S.) 1093; Sturge v. Eastern, &c., Ry. Co., 7 De G., M. & G. 158 (1855); Stevens v. South,

&c., Ry. Co., 9 Hare, 313 (1851); Matthews v. Great Northern, &c., Ry. Co., 28 L. J. Chan. 375 (1859); Corry v. Londonderry, &c., Ry. Co., 29 Beav. 263 (1860); Webb v. Earle, L. R. 20 Eq. 556 (1875); Coates v. Nottingham, &c., Ry. Co., 30 Beav. 86 (1861); Smith v. Cork, &c., Ry. Co., Ir. L. R. 3 Eq. 356 (1869); s. c., 5 Id. 65; Coey v. Belfast, &c., Ry. Co., Ir. Rep. 2 C. L. 112 (1866). But upon the passage in England of the Companies Clauses Act of 1863, 26 & 27 Vict. ch. 16, § 14, it was provided that preference shares or stock shall be entitled to the preference dividend or interest assigned thereto out of the profits of each year in priority to the ordinary shares and stock of the company, but that if in any year there are not profits available for the payments of the full amount or the preferential dividend or interest for that year, no part of the deficiency shall be made good out of the profits of any subsequent year, or out of any other funds of the company. In Henry v. Great Northern Ry. Co., 1 De G. & J.

When arrears are recoverable interest on such arrears may be recovered.¹

Where there was a provision for the payment of a dividend to the holders of the common stock after the payment of the preferred dividend, it was held that arrears of common dividends must be paid next after the arrears of preferred dividends, and before any further preferred dividends could be declared.² And where there is a statutory provision that dividends on the pre-

606, in which the matter of arrears in preferred dividends was elaborately considered, it was urged that a reason why such arrears ought to be held payable out of subsequent profits is that otherwise there would be a temptation to the corporation to set aside profits for improvements when the profits were too small for a dividend on both the common and the preferred shares, or not to set aside enough for improvements in order to make a dividend for both. As illustrating the right to the arrearage, Knight Bruce, L. J., in the opinion in this case, said: "Let us suppose a right to have a tun of wine from a vineyard. Is that the same merely as a right to have a tun of wine from a vintage? I do not think so. In the former case the deficiency of an earlier would have to be supplied by a later vintage; not so, possibly, in the other. Here, as I apprehend, the plaintiffs 'have the vineyard, and not merely the chance of a particular vintage to look to.'" In *Dent v. London Tramways Company*, L. R. 16 Chan. Div. 344 (1880), it was held that the owners of preference shares, the dividend on which was "dependent upon the profits of the particular year only," were entitled to a dividend out of the profits of any year after setting aside a proportionate amount sufficient for the maintenance and repair of the tramway for that year only, and that they were not to be deprived of that dividend in order to make good the sums which in previous years should have been set aside by the company for maintenance, but which had been improperly applied by them in paying dividends. This was a case in which the articles of association provided that no dividends should be declared except out of profits, and that the directors must, before declaring dividends, set aside out of profits a reserve fund for maintenance, repairs, depreciation, and renewals, and it appeared that the company had for several years carried on its business and paid

dividends without setting aside this fund, until the property was worn out. Then the attempt was made by appropriating the total net profits to restore the property at once, and the court held that this could not be done to the prejudice of the interests of the preferred shareowners. *Cf. Nichols v. New York, &c., R. R. Co.*, 15 Fed. Rep. 575 (1883). Where each share in a company was converted into two half shares, one preferred, the other common or deferred, and the holders of the preferred half shares had, in a former year, acquiesced in the declaration of a dividend on the deferred half shares, while there was an arrearage of dividends on the preferred half shares, it was held that, although they had precluded themselves from making any claim to those specific arrears, they had not waived their right to claim subsequent arrears. *Matthews v. Great Northern, &c., Ry. Co.*, 28 L. J. Chan. 375 (1859); *Smith v. Cork, &c., Ry. Co.*, Ir. L. R. 3 Eq. 356 (1868); s. c., 5 Id. 65. And again, where a mortgage was executed upon the property of a corporation for the purpose of raising funds, subsequently to an issue of preferred stock, the mortgage was held to be not in derogation of the rights of the preferred shareowners, and an injunction to restrain the execution of the mortgage was refused. *Garrett v. May*, 19 Md. 177 (1862). So also of mortgage bonds consolidating prior and subsequent indebtedness. *Thompson v. Erie Ry. Co.*, 45 N. Y. 468 (1871); s. c., 11 Abb. Prac. 188; 42 How. Prac. 68. See also *Bailey v. Railroad Co.*, 1 Dill. 174 (1872); s. c., 17 Wall. 96; *St. John v. Erie Ry. Co.*, 10 Blatch. 271 (1874); s. c., 22 Wall. 137; *Richardson v. Vermont, &c., R. R. Co.*, 44 Vt. 613 (1872).

¹ *Boardman v. Lake Shore, &c., R. R. Co.*, 84 N. Y. 157 (1881).

² *Allen v. Londonderry, &c., Ry. Co.*, 25 Week. Rep. 524.

ferred stock shall not exceed a certain rate per cent., then there is no carrying over a deficiency of that per cent.¹

§ 273. *The option to exchange common for preferred shares.*—When the power to issue preferred stock is conferred upon a corporation, it is sometimes provided that under certain conditions the common stock may be exchanged for the preferred stock.² Concerning this option it is to be noted that any time limited is of the very essence of the offer. So where an option was given to holders of the common stock to take a certain number of new shares within a given time, it was held that a shareowner who lived abroad and had no notice of the option until the expiration of the specified time, could not, upon learning of it afterwards, come in and demand the right to purchase the preferred shares.³ So likewise where there was an option within a fixed time to convert loan notes into shares.⁴ And where the time for payment of a series of convertible bonds was extended, it was held that such extension did not extend the time as fixed in the bond within which it might be converted into stock.⁵

§ 274. *Rights of the assignee or transferee of preferred stock in arrears of dividends.*—The transferee or assignee of preferred stock stands, in respect to arrears of dividends, in the shoes of his assignor or transferor. The undeclared arrears of dividends pass to him in the transfer of the stock, unless by the terms of the transfer the arrears are expressly separated from the stock itself and reserved to the transferor, as may be done.⁶ But it has been held that arrears of dividends on preferred shares, not declared, cannot be assigned apart from the stock itself.⁷

§ 275. *"Special stock" in Massachusetts.*—In Massachusetts, incorporated companies are permitted by statute⁸ to issue a pecu-

¹ *Elkins v. Camden, &c., R. R. Co.*, 36 N. J. Eq. 233 (1882).

² New York Session Laws, 1880, chap. 225; *Webb v. Earle*, L. R. 20 Eq. 556 (1875).

³ *Pearson v. London, &c., Ry. Co.*, 14 Sim. 541 (1845).

⁴ *Campbell v. London, &c., Ry. Co.*, 5 Hare, 519 (1846).

⁵ *Muhlenberg v. Phila., &c., R. R. Co.*, 47 Penn. St. 16 (1864).

⁶ *Jermain v. Lake Shore, &c., R. R. Co.*, 91 N. Y. 483 (1883); *Boardman v. Same*, 84 Id. 157 (1881); *Hyatt v. Allen*,

56 Id. 553 (1874); *Manning v. Quicksilver, &c., Co.*, 24 Hun, 361 (1881); *Nichals v. New York, &c., R. R. Co.*, 15 Fed. Rep. 575 (1883); *Coey v. Belfast, &c., Ry. Co.*, Ir. Rep. 2 Com. Law, 112 (1866). But it is otherwise when the dividend has been declared before the transfer. *City of Ohio v. Cleveland, &c., R. R. Co.*, 6 Ohio St. 489 (1856).

⁷ *Manning v. Quicksilver Mining Co.*, 24 Hun, 361 (1881).

⁸ Sts. 1855, ch. 290; 1870, ch. 224, §§ 25, 39, cl. 4; Pub. Sts. ch. 106, §§ 42, 61, cl. 3.

liar kind of stock, known as "special stock." It is something essentially different from preferred stock.¹ Its essential characteristics are that it is limited in amount to two-fifths of the actual capital; it is subject to redemption by the corporation at par after a fixed time, to be expressed in the certificate; the corporation is bound to pay a fixed half-yearly sum, or dividend, upon it as a debt; the holders of it are in no event liable for the debts of the corporation beyond their stock, and the issue of this special stock makes all the general stockholders liable for all debts and contracts of the corporation until the special stock is fully redeemed.² Preferred stock is, therefore, plainly something quite different from this. Authority to issue special stock is conferred, as we have seen, by general statute; while in Massachusetts, authority to issue preferred stock is not conferred in express terms by any general statute, but special statutes have from time to time authorized individual companies to issue preferred stock with various special provisions.³ Special stock can be issued only by a vote of three-fourths of the general stockholders of the company, at a meeting duly called for that purpose.⁴ The guarantee of dividends of special stock in Massachusetts is an absolute one, and not in any degree conditional upon the earning of sufficient profits by the corporation.⁵

¹ *American Tube Works v. Boston, &c., Co.*, 139 Mass. 5 (1885).

² The statutes cited *supra*; *American Tube Works v. Boston, &c., Co.*, 139 Mass. 5 (1885).

³ *E. g.* Sts. 1853, ch. 1; 1855, ch. 143; 1877, ch. 170; 1878, ch. 138; 1882, ch. 177.

⁴ Sts. 1870, ch. 224, § 25. And the corporation must have a clerk, who is sworn, and who acts as recorder at such meeting. Sts. 1870, ch. 224, §§ 15, 18; Pub. Sts. ch. 106, §§ 23, 26. See also *Reed v. Boston Machine Co.*, 141 Mass. 454 (1886). This special stock is declared to be "a peculiar kind of stock, distinctly provided for by statute," and it is important that the marked distinction between preferred stock, as usually understood, and special stock, as authorized by the statutes cited in the notes, be kept plainly in view. *American Tube Works v. Boston, &c., Co.*, 139 Mass. 5 (1885).

It was held, in accordance with this view, in the case last cited, that a vote of a corporation to issue special stock, at a

meeting called to consider whether the corporation will issue preferred stock, is invalid; that a vote to issue special stock is invalid if the record of the meeting fails to show that three-fourths of the general shareholders voted for such issue; that the court will not presume, because the record showed that more than three-fourths of the shareholders were present at the meeting; that, therefore, three-fourths or more voted for the issue of special stock; and that a holder of special stock, which is illegally issued, cannot, by estoppel or otherwise, become a member of the corporation in respect of such shares.

⁵ *Williams v. Parker*, 136 Mass. 204 (1894). See also *Allen v. Herrick*, 81 Id. 274 (1860). It is said that the stock authorized by these statutes—*i. e.*, special stock—has some of the characteristics of stock and some of the characteristics of a debt of the corporation; that when the net earnings of the company are not sufficient to pay the dividends, the company shall make good the difference out of any

§ 276. *Remedies of shareholders herein.*—The rights of preferred stockholders with respect to their dividends are protected in equity by injunction or by other equitable remedies.¹ Equity will protect the prior right of such shareholders in the distribution of the profits of the company.² Specific performance in a proper case will be decreed.³ But an action at law cannot be maintained where the dividend sought to be reached has not been actually declared.⁴ Nor has a court of equity jurisdiction in the case of a foreign corporation, having neither officer nor place of business in the State.⁵ Where a corporation, having issued preferred stock, is merged into a new corporation by consolidation, the preferred shareholders of the old corporation may prosecute a suit for dividends against the new corporation.⁶ In an action to compel the corporate manager to declare a preferred dividend, the common stockholders are proper but not necessary parties.⁷

§ 277. *Interest-bearing stocks.*—Occasionally, instead of issuing preferred stock, a corporation issues ordinary common stock, together with a promise that the corporation will pay interest thereon. Such a promise is generally lawful, and may be enforced as a contract in the nature of an agreement to pay a dividend.⁸ This promise to pay interest on stock will be construed as an undertaking on the part of the corporation to pay when the corporate finances are in such a condition that a legal dividend might properly be declared. It is a lawful contract, however, only when it is to be interpreted as requiring payment from profits alone.⁹ Any contract on the part of a corporation to pay

property it has, and that it is the general legislative policy of the State to regard holders of this stock creditors of the corporation for the dividends guaranteed, which have become payable. *Williams v. Parker*, 136 Mass. 204 (1884).

¹ *Boardman v. Lake Shore, &c., R. R. Co.*, 84 N. Y. 157 (1881); *Ellsworth v. New York, &c., R. R. Co.*, 98 N. Y. 648 (1885); s. c. 19 Week. Dig. 211; *Henry v. Great, &c., Ry. Co.*, 4 Kay & J. 1 (1857).

² *Sturge v. Eastern, &c., Ry. Co.*, 7 De G., M., & G. 158 (1855); *Smith v. Cork, &c., Ry. Co.*, Ir. Rep. 3 Eq. 356 (1869); *Bailey v. Hannibal, &c., R. R. Co.*, 1 Dill. 174 (1871); *Prouty v. Michigan, &c., R. R. Co.*, 1 Hun, 655 (1873); *Thompson v. Erie Ry. Co.*, 45 N. Y. 468 (1871).

³ *Boardman v. Lake Erie, &c., R. R. Co.*, 84 N. Y. 157 (1881).

⁴ *Williston v. Michigan, &c., R. R. Co.*, 95 Mass. 400 (1866).

⁵ *Williston v. Michigan, &c., R. R. Co.*, *supra*.

⁶ *Boardman v. Lake Shore, &c., R. R. Co.*, 84 N. Y. 157 (1881); *Chase v. Vanderbilt*, 62 Id. 307 (1875).

⁷ *Thompson v. Erie R. Co.*, 45 N. Y. 468 (1871). *Cf. Chase v. Vanderbilt*, 62 Id. 307 (1875).

⁸ *Barnard v. Vermont, &c., R. R. Co.*, 89 Mass. 512 (1863).

⁹ *Miller v. Pittsburgh, &c., R. R. Co.*, 40 Penn. St. 237 (1861); *Richardson v. Vermont, &c., R. R. Co.*, 44 Vt. 613 (1872); *Cunningham v. Same*, 78 Mass. 411 (1859); *McLoughlin v. Detroit, &c., R. R. Co.*, 8 Mich. 100 (1860); *City of*

interest or dividends to its shareholders, without reference to the ability of the company to pay them out of its earnings, is wholly illegal and void.¹ Accordingly, it is illegal and contrary to public policy to allow a corporation to pay interest on interest-bearing stock out of the capital stock of the corporation, or while there are debts due by the corporation which should be immediately paid.² Moreover, the directors or corporate officers paying interest on stock out of the capital stock, are jointly and severally liable to refund the amounts so paid out.³ A railway company may lawfully receive subscriptions to its capital stock upon the condition to pay interest thereon as soon as the amount of the subscription shall have been paid in, and until the completion of the road, or of some part thereof, or until the road shall have been put in operation.⁴ It has been held that stipu-

Ohio *v.* Cleveland, &c., R. R. Co., 6 Ohio St. 489 (1856); Evansville, &c., R. R. Co. *v.* City of Evansville, 15 Ind. 395; Rutland R. R. Co. *v.* Thrall, 35 Vt. 543 (1863); Wright *v.* Vermont, &c., R. R. Co., 66 Mass. 68 (1853); Waterman *v.* Troy, &c., R. R. Co., 74 Id. 433; Barnard *v.* Vermont, &c., R. R. Co., 89 Id. 512 (1863).

¹ Painesville, &c., R. R. Co. *v.* King, 17 Ohio St. 534 (1867); Pittsburgh, &c., R. R. Co. *v.* County of Allegheny, 63 Penn. St. 126 (1869); Miller *v.* Pittsburgh, &c., R. R. Co., 40 Id. 237 (1861); Lockhart *v.* Van Alstyne, 31 Mich. 76 (1875); Troy, &c., R. R. Co. *v.* Tibbits, 18 Barb. 297 (1854); McDougall *v.* Jersey, &c., Co., 2 Hem. & M. 528 (1864); Salisbury *v.* Metropolitan Ry. Co., 38 L. J. (N. S.) Ch. 249 (1869).

² Pittsburgh, &c., R. L. Co. *v.* County of Allegheny, 63 Penn. St. 126 (1869); Painesville, &c., R. R. Co. *v.* King, 17 Ohio St. 534 (1867); Salisbury *v.* Metropolitan, &c., Ry. Co., 38 L. J. (N. S.) Ch. 249 (1869); *In re* National, &c., Co., 10 L. R. Chan. Div. 118 (1878); McDougall *v.* Jersey, &c., Co., 10 Jur. (N. S.) 1043 (1864). *Cf.* Bardwell *v.* Sheffield, &c., Co., L. R. 14 Eq. Cas. 517 (1872). And a payment of interest on stock before profits are earned is in violation of a statute prohibiting dividends from capital stock. Pittsburgh, &c., R. R. Co. *v.* County of Allegheny, 63 Penn. St. 126 (1869).

³ *Re* National, &c., Co., 10 L. R. Chan. Div. 118 (1878).

⁴ Milwaukee, &c., R. R. Co. *v.* Field,

12 Wis. 340 (1860); Racine County Bank *v.* Ayers, 12 Id. 512 (1860); Miller *v.* Pittsburgh, &c., R. R. Co., 40 Penn. St. 237 (1861); Rutland, &c., R. R. Co. *v.* Thrall, 35 Vt. 536 (1863). But in Pennsylvania such an undertaking on the part of a corporation is pronounced "foolish." In Miller *v.* Pittsburgh, &c., R. R. Co., *supra*, Woodward, J., says: "This company conformed to the foolish practice of receiving subscriptions on a guarantee that they would pay interest on stock 'as soon as paid in' until the road is finished. When it is considered that railway companies are joint-stock associations, and depend on borrowing most of the money they expect to expend, the absurdity of borrowing money to pay interest to themselves is self-evident. . . . No intelligent stockholder who has the interest of the enterprise at heart ought to accept or insist on such a condition." Such a condition, if it contemplated the payment of the interest before the company had accumulated earnings proper to be appropriated to a dividend would, as we have seen, be void. And when the condition does not specify any time of payment, the interest can only be payable when a sufficient amount of net profits have been earned. Rutland, &c., R. R. Co. *v.* Thrall, 35 Vt. 543 (1863); Waterman *v.* Troy, &c., R. R. Co., 74 Mass. 433 (1857). Hence it may be concluded that the only effect of an agreement by the corporation to pay such interest is to enable those stockholders, with whom the agreement is made, to claim a dividend and arrears of dividend before other stockholders re-

lated interest on stock cannot become a debt payable absolutely.¹ The right of a subscriber drawing interest on his stock to participate in elections and general corporate meetings, and to exercise generally the rights of a shareowner, is the same as that of other stockholders.² His *status* as a stockholder is not affected by the mere consideration that he is to be paid interest upon his investment. Payment of interest on stock, being in its essence only a form of dividend, is enforceable in a Court of Chancery only when a dividend would be ordered. The same rules prevail in the one case as in the other. There must be *bona fide* profits, and funds sufficient for the payment equally of all such stockholders in addition to that necessary for current expenses, the payment of floating debts due, and a reasonable sum for contingencies.³

§ 278. *Rights of preferred shareowners on dissolution.*—Upon the dissolution of a corporation, and the distribution of its assets among the shareholders after the payment of the corporate indebtedness, it is the settled rule of law that, in the absence of any statutory provision, preferred shareholders have no priority over common stockholders. Their stock was preferred in respect of dividends, and not in reference to the capital stock. The assets of the corporation are to be distributed as though no preferred shares had been issued. The preferred shareholder in the distribution becomes a common shareholder.⁴ Where, however, a preference as to capital has been expressly contracted for,⁵ or is given by a statute,⁶ the rule is, of course, otherwise.⁷ This, how-

ceive anything. This is nothing more nor less than a preferred dividend.

¹ *Barnard v. Vermont, &c.*, R. R. Co., 89 Mass. 512 (1863). On the other hand, it has been held that the relation of debtor and creditor is created to the extent of the interest stipulated for. *McLoughlin v. Detroit, &c.*, R. R. Co., 8 Mich. 100 (1864).

² *McLoughlin v. Detroit, &c.*, R. R. Co., *supra*.

³ *Richardson v. Vermont, &c.*, R. R. Co., 44 Vt. 613 (1872); *Barnard v. Id.*, 89 Mass. 512 (1863).

⁴ *McGregor v. Home Ins. Co.*, 33 N.J. Eq. 181 (1880); *In re London India Rubber Co.*, L. R. 5 Eq. 519 (1864).

⁵ *Re Bangor, &c., Slate Co.*, L. R. 20 Eq. 59 (1875).

⁶ *McGregor v. Home Ins. Co.*, 33 N.J. Eq. 181 (1880).

⁷ Where a corporation was dissolved by consolidation with another, it was held that there might be a preference in the distribution of the assets of the old corporation. *Griffith v. Paget*, L. R. 6 Chan. Div. 511 (1877); s. o. 25 W. R. 523. The *status* of the holders of preferred shares in the distribution of the capital on the winding up of the company, in the absence of any statute designating how the assets are to be apportioned, or of any provision in the contract itself, is well set out in the decision in the case of *McGregor v. Home Insurance Co.*, *supra*. It amounts to this. While the concern is going, if there are any profits earned, the preferred shareowners are to be paid. If

ever, is not generally the case, and upon dissolution all the stockholders, both common and preferred, share equally in the distribution of assets.

there be no profits they get nothing, for they are not creditors, but rather partners. On the dissolution, the profits are at an end. The only fund to which they have a right to look for profit ceases to earn anything. The capital remains, but inasmuch as the preferred shareholders could not draw on the capital during the life of the company, so they are not entitled to any preference when it is defunct. This rule was first laid down, it seems, by Malins, V. C. *In re London Rubber Co.*, L. R. 5 Eq. 519 (1867). And it has not been questioned either in this country, *McGregor v. Home Ins. Co.*, 33 N. J. Eq. 181 (1880), or in England. *Griffith v. Paget*, L. R. 6 Chan. Div. 511 (1877).

In the case last cited, the Master of the Rolls luminously said: "All these companies are commercial partnerships, and are, in the absence of express provisions, statutory or otherwise, subject to the same considerations. If in an ordinary commercial partnership one or more of the partners has a larger share of the profits than is the proportion borne by his share of the capital to the capital of the others, whether on account of his services (which is the more frequent ground, in cases of partnership, for giving the larger share), or on account of the services of others formerly given to the partnership, which is sometimes done, especially in the case of a second or third generation, that privilege ceases when the partnership is dissolved. If you give an annuity out of profits to a widow during the continuance of the partnership,

she having no share of the capital, of course that, *ex vi termini*, will come to an end at the dissolution of the partnership. If you give a managing partner a salary, or a larger share of profits than his proportion of the capital, of course, at the dissolution the management comes to an end and his larger share of profits.

"But in the ordinary case, when the profits are unequally divided—that is unequally, as regards the share of capital—the same rule prevails, and that is quite independently of the circumstance whether the excess of profits is given for services, or given to a sleeping partner for the use of his name or otherwise.

"When the partnership comes to an end, the right to the share of profits comes to an end also; and you distribute the assets, after providing for the profits earned up to the time of the dissolution, in proportion to the partners' shares of the partnership capital. That is the general rule of law in a commercial partnership. Therefore you would distribute the assets simply in proportion to the capital. This is a commercial partnership subject to certain statutory limits. Therefore, if there were no provision to be found anywhere, you would distribute the assets in proportion to the capital, and the mere arrangement for the division of profits *inter se*, during the continuance of the partnership, would have no direct bearing on the division of the capital as distinguished from profits earned up to the time of the dissolution after the dissolution of the company."

CHAPTER XVII.

INCREASE AND REDUCTION OF THE CAPITAL STOCK AND OVERISSUED STOCK

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| <p>§ 279. Introductory.</p> <p>280. Power of the legislature to authorize an increase or reduction.</p> <p>281. Power of the corporate authorities to increase or reduce the capital stock.</p> <p>282. Effect of purchase by a corporation of shares of its own stock.</p> <p>283. The issue of bonds convertible into stock.</p> <p>284. Power of a court to direct an increase or reduction.</p> <p>285. Shareholders, not directors, should authorize the increase.</p> <p>286. Pre-emptive right of the old stockholders to buy the new stock.</p> <p>287. Issue of an increase of stock by a stock dividend.</p> <p>288. Liability of the shareholder upon an increase of the capital stock.</p> <p>289. Right and liability of the shareholder upon a reduction of the capital stock.</p> | <p>§ 290. Changes in the number or par value of the shares.</p> <p>291. Unauthorized increase of stock may amount to overissued stock.</p> <p>292. Overissued stock is absolutely void.</p> <p>293. Liability of the corporation on overissued stock.</p> <p>294. Defenses of the corporation to such actions.</p> <p>295. Personal liability of the officers of the corporation on overissued stock.</p> <p>296. Liability of the vendor of overissued stock.</p> <p>297. Equity will enjoin voting, transferring, and dividends, on such stock, and will adjust the right of all parties.</p> <p>298. Subscriber's right to defeat a subscription to overissued stock, and to recover back money paid thereon.</p> |
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§ 279. *Introductory.*—In general, the capital stock of all incorporated companies, is definitely stated by the charter which makes it a corporation. When such a company is created by special act of the legislature, the amount of the capital stock is almost universally fixed by the charter of the incorporation. And when the company is organized under one of the general incorporating acts, which have been enacted in all the States of the Union, the act itself generally provides that the amount of the capital stock be fixed and specified in the articles of association. This prescribes and limits the amount of the stock as fully as though it had been fixed by a special charter from the legislature. It frequently happens, however, in the progress of the corporate enterprise, subsequently to the incorporation, that the capital stock is found to be too large or too small for the demands of the business, and there is a desire to increase or reduce the capital stock as fixed by the charter. This can lawfully be done only

under certain prescribed conditions and limitations, which it is proposed in this chapter to consider. The large number of cases on this subject, show that the attempt to make this change in the amount of the capital stock, has been a fruitful source of mistakes and litigation, and that in undertaking it, a corporation is liable to commit illegal or irregular acts, which give rise to complications, difficulties, and loss to the stockholders.

§ 280. *Power of the legislature to authorize an increase or reduction.*—It is plainly within the proper province of the legislature, upon granting a charter of incorporation, to fix the amount of the capital stock of the company incorporated. But it is a serious question, whether the legislature may amend a charter, so as to allow an increase or reduction of the capital stock, as against the protest of one or more dissenting stockholders. The original charter is clearly a contract between the incorporators and the State. No material change can be made in that charter except by the consent of both parties—the State on the one side, and all the incorporators or stockholders on the other. If the increase or reduction, as authorized by a statute, passed subsequently to the vesting of the charter, is a material change of that charter, then a unanimous consent of the stockholders is necessary to its validity.¹

Where, however, as is usual in most charters which have been granted in recent years, the legislature possesses the reserved power to alter, amend, or repeal the charter of the corporation, then a statute authorizing an increase or reduction of the capital stock may at any time be passed, without impairing the obligation of the contract between the State and the incorporators, and the shareholders will not be heard to object.² Corporate credit-

¹ See Chapter on Amendments to Charter. In *Bergman v. St. Paul Mutual Building Association*, 29 Minn. 275 (1882), it is held that the corporation cannot arbitrarily, by a by-law, compel the shareholder to sell his stock to the corporation in order that it may be retired. And that a voluntary consent by the shareholder to the retirement of part of his stock is no waiver of his right to object to the retirement of the remainder.

² *Buffalo, &c., R. R. Co. v. Dudley*, 14 N. Y. 336 (1856); *Joslyn v. Pacific Mail Steamship Co.*, 12 Abb. Prac. (N. S.) 329 (1872). Thus, where the powers of the

corporation were extended by a subsequent act of the legislature, passed by virtue of the reserved power in the charter, it was held that the subscribers to the capital stock were not thereby discharged. *Peoria, &c., R. R. Co. v. Elting*, 17 Ill. 429 (1856). And if such a statutory amendment be accepted by the directors of the corporation, the subscribers to the stock are not released. *Illinois River R. R. Co. v. Zimmer*, 20 Ill. 654 (1858). Where, however, the increase of capital stock is so great as to change essentially the liability of the shareholder, and to impose upon him, in reality, a new

ors may, however, have such vested rights in the corporate property, that the legislature cannot constitutionally authorize the reduction of the capital stock, in prejudice of their rights as to antecedent corporate indebtedness.¹

Sometimes provision is made for the increase or reduction of the amount of the capital stock of incorporated companies, by a general statutory provision in the statute authorizing the incorporation.² Authority to increase the capital stock of a corporation may undoubtedly be conferred by a law passed subsequently to the charter, but such a law is valid only when accepted by the stockholders. This assent may either be inferred from subsequent acquiescence, or it may be given by express vote of the shareholders in meeting assembled.³

§ 281. *Power of the corporate authorities to increase or reduce the capital stock.*—In the absence of express authority from the State, a corporation has no power whatsoever to increase or reduce the amount of its stock, and any attempt upon the part of the corporation, either by the corporate officers or by the stockholders, to do so, is wholly illegal and void.⁴ Accordingly it is

contract, the increase will operate to discharge such of the subscribers to the capital stock as do not assent to it, or subsequently acquiesce. *Hughes v. Antietam, &c., Co.*, 34 Md. 316 (1870). The same rule prevails in the case of a reduction of the capital stock. *Oldtown, &c., R. R. Co. v. Veazie*, 39 Me. 571 (1855). But *cf.* Chapter on Amendments.

¹ *Re State Insurance Co.*, 14 Fed. Rep. 28 (1882); s. o. 11 Biss. 301; *Palfrey v. Paulding*, 7 La. Ann. 363 (1852); *Re Telegraph Construction Co.*, L. R., 10 Eq. 384 (1870); *Cóoper v. Frederick*, 9 Ala. 742 (1846); *Morawetz on Corp.* (2d edition), §§ 833, 851. *In re Credit Fancier of England*, L. R., 11 Eq. 356 (1871). And in England a corporate creditor may enjoin a distribution of assets on reduction, among the stockholders, until his claim is secured. *In re Telegraph Construction Co.*, L. R., 10 Eq. 384 (1870).

² New York Session Laws, 1848, chap. 40, §§ 20, 21; 1850, chap. 140, § 9; 1878, chap. 264; Rev. Stat. of Ohio (1886), §§ 3262–3264; *Brightley's Purdon's Digest*, Laws of Penn. (1883), page 343, §§ 33, 34; page 348, § 55 *et seq.* (Laws of Penn., April 29, 1874); Pub. Stat. of Mass. (1882), ch. 106, § 34; ch.

112, § 60; Ann. Stat. of Ill., Starr & Curtis (1885), ch. 32, § 50; ch. 114, § 15; Rev. of N. J. (1877), page 181, § 24; page 1290, § 29. In Louisiana the constitution and laws make express provision for the increase of the capital stock of incorporated companies. Constitution of La., art. 239; Laws of La. (1882), art. 26; Rev. Stat. of La., § 693. But no provision is anywhere made in the constitution or by statute for the reduction of capital. The courts, therefore, conclude that the omission was intentional, and that corporations in that State, in consequence, can have no power to reduce their stock. *Seignouret v. Home Insurance Co.*, 24 Fed. Rep. 332 (1885).

³ *Railway Company v. Allenton*, 18 Wall. 233, 235 (1873).

⁴ *Scoville v. Thayer*, 105 U. S. 143, 148 (1881); *Knowlton v. Congress, &c., Spring Co.*, 14 Blatchf. 364 (1877); *Grangers Life, &c., Insurance Co. v. Kamper*, 73 Ala. 325 (1882); *Moses v. Ocoee Bank*, 1 Lea (Tenn.), 398 (1878); *Ferris v. Ludlow*, 7 Ind. 517 (1856); *Sutherland v. Olcott*, 95 N. Y. 93, 100 (1884); *New York, &c., R. R. Co. v. Schuyler*, 34 Id. 30 (1865); *Mechanics Bank v. New York, &c., R. R. Co.*, 13 Id. 599 (1856); *Lathrop*

not competent for a corporation, having a fixed capital stock to reduce that capital to the amount actually paid in;¹ nor, by a by-law, to authorize the directors to reduce the par value of the shares.²

Where the attempted increase or reduction of the stock is illegal and unauthorized, not even the unanimous assent and agreement of all the parties concerned will legalize it.³ An authority to reduce the number of shares cannot be inferred from the authority to increase, and a reduction with no other warrant of authority than a right to increase will be held void.⁴ Where subscriptions are made to an unauthorized increase of

v. Kneeland, 46 Barb. 432 (1866); *Salem Mill Dam Corporation v. Ropes*, 6 Pick. 23 (1827). "If," says Parker, C. J., in the case last cited, "a corporation is created with a fund, limited by the act, it cannot enlarge or diminish that fund, but by a license from the legislature, and if the capital stock is parcelled out into a fixed number of shares, this cannot be changed by the corporation." *Acc. Stace & Worth's Case*, L. R., 4 Chan. 682 (1869); *Morawetz on Corp.* (2d edition), § 434.

¹ *Droitwich Patent Salt Co. v. Curzon*, L. R., 3 Exch. 35, 42 (1867). But an issue of stock to the amount of the subscriber's payments, and a cancellation of the balance of his subscription, were held not to constitute a reduction of the capital stock *pro tanto*. *Chetlain v. Republic Life Insurance Co.*, 86 Ill. 220 (1877). In England it is the rule that when the assets are already reduced by losses, the corporation cannot effect a reduction of the capital stock, so as to cover up the losses. *In re Ebbw Vale Steel, Iron & Coal Co.*, L. R., 4 Chan. Div. 827 (1876). And yet it should seem that a greater fraud would be worked upon the public by continuing business with an impaired capital, than to reduce it openly to what it actually is. *Cf. In re Kirkstall Brewery Co.*, L. R., 5 Chan. Div. 535 (1877).

² *In re Financial Corporation*, L. R., 2 Chan. 714 (1867). "The amount of the shares is properly part of the constitution of the company," so that an unauthorized reduction is simply void, and the stock and capital remain the same as before such attempted reduction. *Smith v. Goldsworthy*, 4 Q. B. 430 (1843); *Sewell's Case*, L. R., 3 Chan. 131 (1868). But in *Ambergate, Nottingham & Boston & Eastern Ry. Co. v. Mitchell*, 4 Exch. 540 (1849); s. c. 6 Eng. Ry. Cases, 234, it

was held that a reduction by the company of its shares, from £25 to £20, was, in the absence of any act prohibiting it, lawful and valid. An increase, however, in the size of the shares—doubling their par value—is such a change as will release a non-assenting subscriber to the stock to the extent of such increase. He will be liable on his subscription for shares of the original value only. *In re European Central Ry. Co.*, L. R., 8 Eq. 438 (1869). And a distribution of part of the capital stock among the shareholders proportionally, is an unauthorized reduction, and the stock will be ordered to be returned. *Holmes v. Newcastle, upon Tyne Abattoir Co.*, 45 L. J. (Chan.) 383 (1875). It has been held allowable, however, for the company to allow the holders of paid up shares to return them, and take in exchange shares of double the par value as half paid up, and *vice versa*; both kinds of stock being authorized. *Teasdale's Case*, L. R., 9 Chan. 54 (1873). Shareholders cannot, however, be compelled to make such an exchange.

³ "The officers, directors, and stockholders of an incorporated company, cannot, even by an unanimous agreement, made under an honest misapprehension of their powers, increase the capital of the company." *People v. Parker Vein Coal Co.*, 10 How. Prac. 543 (1854). Irregularity of notice of meeting is fatal. *Matter of Wheeler*, 2 Abb. Prac. (N. S.) 361. If the statute requires a publication of notice of the intended increase, such publication must be made. It cannot be waived, even by unanimous consent of the stockholders. The public are entitled to knowledge of the increase. *State v. McGrath*, 86 Mo. 239 (1886).

⁴ *Sutherland v. Alcott*, 95 N. Y. 93 (1884).

stock, which is subsequently and legally validated, in an authorized manner, the subscribers, if they acquiesce, are bound.¹

If the charter of the corporation provides that the capital stock shall not be less than a specified sum, nor greater than another specified sum, the corporation may commence business with less than the latter sum, and afterwards increase the capital until the limit is reached.²

An injunction is the proper remedy to prevent an illegal increase or reduction of the capital stock of a corporation. But an injunction against the issue of new stock by a foreign corporation, will be dissolved, where the courts of the State where the corporation was created decide such issue of stock to be legal.³

§ 282. *Effect of purchase by a corporation of shares of its own stock.*—If a corporation have power to reduce its capital stock it may unquestionably do so by purchasing and retiring a portion of its shares.⁴ Whether such a purchase by a corpora-

¹ Sewell's Case, L. R., 3 Chan. 131 (1868). And where an increase was authorized by law, but had been made in an irregular manner, so that the new stock was apparently legal, but might have been annulled by an action by the Attorney-General, a subscriber to such stock who paid the purchase price in part, and received the certificate, and subsequently voted on the stock at corporate meetings, was held estopped to question the regularity of the issue, in an action by the receiver of the corporation to collect the unpaid subscription. *Chubb v. Upton*, 95 U. S. 665 (1877); *s. p. Upton v. Jackson*, 1 Flippin, 413; *Kansas City Hotel Co. v. Hunt*, 57 Mo. 126 (1874). In such a case the State alone can properly raise the question whether the corporate stock had been regularly and lawfully increased. *Pullman v. Upton*, 96 U. S. 329 (1877). See *Clarke v. Thomas*, 34 Ohio St. 46; *Matter of the Reciprocity Bank*, 22 N. Y. 9 (1860); *Kansas City Hotel Co. v. Harria*, 51 Mo. 464 (1873). But where a subscription is made, and the amount of it or any part of it paid in, on the supposition that the shares taken are part of a lawful increase of the stock, the money so paid may be recovered back, if for any reason it turns out that the increase was not lawfully made. *Knowlton v. Congress & Empire Spring Co.*, 14 Blatchf. 364 (1877); *s. c. aff'd sub nom. Spring Company v. Knowlton*, 103 U. S. 49 (1880).

[Compare with these cases the dissenting opinion of Dwight, C., in *Knowlton v. Congress & Empire Spring Co.*, 57 N. Y. 518, 540 (1874).] See also *Peckham v. Smith*, 9 How. Prac. 436 (1854). And where the capital stock had been unlawfully increased, a promissory note given in payment for shares of stock could not, it was held, be collected, for the reason that it was impossible to show that the stock delivered to the purchaser was not part of the illegal issue. *Merrill v. Gamble*, 46 Iowa, 615 (1877); *Merrill v. Beaver*, 46 Id. 646 (1877). But otherwise if stock unquestionably valid was delivered. *Merrill v. Beaver*, 50 Iowa, 404 (1879).

² *Gray v. Portland Bank*, 3 Mass. 364 (1807). *Acc. Somersct. &c., R. R. Co. v. Cushing*, 45 Me. 524 (1858). In the case last cited, it is held that where the number of shares is not fixed by charter, the directors or shareholders must fix it before an assessment can be levied, and that then, if the number fixed is greater than the number taken, it may be reduced subsequently.

³ *O'Brien v. Chicago, Rock Island & Pacific R. R. Co.*, 53 Barb. 568 (1868). An increase of the capital stock without warrant of authority is denominated an overissue of stock—a subject fully considered in the succeeding sections of this chapter *q. v.*

⁴ *State v. Smith*, 48 Vt. 266 (1876); *City Bank of Columbus v. Bruce*, 17 N.

tion will operate to diminish the capital stock is a question of intention. If a reduction is authorized by charter or by statute, and the formalities of making the reduction have been complied with, and the proper corporate authorities purchase for the corporation shares of its own stock and consider the capital stock thereby reduced, the law holds that a reduction of the capital stock is thereby made. But if any of these elements are wanting, then no reduction is effected, and the corporation may at any time sell and reissue the stock.¹ Hence a mere transfer of shares to the corporation, whether the corporation assumes to buy the stock or the shareholders simply to surrender it, will in no case constitute a reduction when the corporation lacks authority from the legislature to reduce its capital. Even if the shareholder is held to be released, by such a transfer, still the stock survives and subsists. The corporation is merely the holder of it, and may sell and reissue it at any time.²

Y. 507 (1858); *Williams v. Savage Manfg. Co.*, 3 Md. Chan. 418 (1851); *Taylor v. Miami Exporting Co.*, 6 Ohio, 176 (1833). In *Currier v. Lebanon Slate Co.*, 56 N. H. 262 (1875), it is held that where a corporation has legislative authority to reduce its capital this "may be done by refunding to its stockholders a definite portion of each share, or by the surrender and extinguishment of the required number of shares." But that it cannot be accomplished "by the purchase and extinguishment of a portion of its shares without the consent and against the protest of any of its stockholders, when such purchase or extinguishment would operate for the relief and benefit of the stockholders from whom the stock is purchased, and will increase the liability of the remaining stockholders." And there is added the statement that "If the corporation desire to increase its capital, this may be done by the issue of new shares, or by increasing the par value of the old." *Cf. Howell v. Chicago, &c. R. R. Co.*, 51 Barb. 378 (1868).

¹ Same cases. The purchase by a corporation, of its own stock, does not necessarily decrease the capital stock. "It might or might not have that effect at the option of the company, and would require, I think, some manifestation of such an intent to produce that result." Such stock may be reissued at any time. *City Bk. of Columbus v. Bruce*, 17 N. Y. 507 (1858).

² *Williams v. Savage Manfg. Co.*, 3 Md. Chan. 418 (1851); *American Railroad Frog Co. v. Haven*, 101 Mass. 398 (1869); *Taylor v. Miami Exporting Co.*, 6 Ohio, 176 (1833); *Chetlain v. Republic Life Insurance Co.*, 86 Ill. 220 (1877). *Cf. Currier v. Lebanon Slate Co.*, 56 N. H. 262 (1875). In some early cases a transfer to the corporation seems to have been regarded as a reduction of the capital stock *pro tanto*. *Percy v. Millaudon*, 3 La. 568, 587 (1832).

In *Taylor v. Miami Exporting Co.*, *supra*, it is held that a banking corporation might accept from a shareholder his stock in payment of a debt due from him to the bank, and that a court of equity would not, after a lapse of several years, compel the shareholder to redeem the stock. In the same case it is also held, where a shareholder takes stock from the corporation, buying and paying for it merely for the purpose of multiplying his vote at an impending election, accepts the certificate, votes on the stock, and then immediately returns the stock to the corporation and gets a return of his money, that equity will not compel him subsequently to refund the money, and accept the stock, it not appearing that any one was injured by the transaction. Upon this point compare *State v. Smith*, 48 Vt. 266 (1876). As a general rule, to which there are few if any exceptions, a stockholder who conveys or assigns his shares to the corporation, without refer-

§ 283. *The issue of bonds convertible into stock.*—Where the charter of a railway corporation authorizes the issue of bonds, convertible at the option of the holder into stock, the directors of the company have power to issue such bonds in the name of the corporation. Such an issue may be made, even though, if the bonds were converted into stock, the capital stock would thereby be increased beyond the amount fixed by the charter. The statute or charter authorizing such an issue of bonds, is held to thereby authorize, by necessary implication, the right to increase the capital stock to the extent required in the fulfilment of the contract to allow the bonds to be converted into stock.¹ The issue of a bond convertible into stock has precisely the same effect as issuing stock, and the sale of such a bond at a discount is unlawful.² The holder of the bonds may demand stock therefor, at any time, and even though the demand is made just before a dividend is declared, he is entitled to the stock and dividend.³

§ 284. *The power of a court to direct an increase or reduction.*—The courts have no power by mandate or decree, or in any

ence to the intent or object of the transfer, and receives in exchange a portion of the capital stock, holds the money so received subject to the superior equities of corporate creditors, which is to say, he is trustee for the creditors *quoad hoc*. *Crandall v. Lincoln*, 52 Conn. 73, 100 (1884). *Cf. Zulueta's Claim*, L. R. 5 Chan. 444 (1870). See also Chapter XIX.

In *Hartridge v. Rockwell*, R. M. Charlton (Ga.), 260 (1828), it is held that directors who purchase stock of the corporation for the account of the corporation and sell it again, neither increase nor diminish the amount of the stock thereby, "since the stock represents so much of the capital as was invested in its purchase, and when sold the money then stands in the place of the stock." It is not within the power of the directors to diminish the actual capital of the corporation by releasing a portion of the stockholders, or by canceling a portion of the stock of each shareholder. Such a proceeding would be in fraud of the rights of creditors and other shareholders. *Gill v. Balis*, 72 Mo. 424 (1880). See also Ch. X, §§ 167-170. Such a transaction, however, even if valid, would not reduce the capital stock. It would merely reduce the number of shares which were supposed to be subscribed for. Fu-

ture subscriptions could be taken to the extent of those released herein.

¹ *Ramsey v. Erie Ry. Co.*, 38 How. Pr. 193, 216 (1869); *Belmont v. Erie Ry. Co.*, 52 Barb. 637, 669 (1869). *Cf. Jenks v. Cent. R. R. Co.*, cited 52 Barb. 637, 675; *Heath v. Erie Ry. Co.*, 8 Blatchf. 347; *People v. Erie Ry. Co.*, 36 How. Pr. 129 (1868); *Ramsey v. Gould*, 57 Barb. 398 (1870); *s. c.* 8 Abb. Prac. (N. S.) 174 (1870); *Pratt v. American Bell Telephone Co.* (Mass. 1886), 12 Am. & Eng. Corp. Cas. 110.

² Where, however, a corporation has power to increase its capital stock, it may issue bonds at 50 per cent. of their par value, convertible into stock upon payment of the other 50 per cent. *Van Allen v. Ill. Central R. R. Co.*, 7 Bosw. (N. Y.) 515 (1861).

³ *Jones v. Terre Haute, &c. R. R. Co.*, 57 N. Y. 196 (1874). The reverse of this rule is also true, and it is held in New York that a corporation, with authority to increase its capital stock, may lawfully issue new shares and receive in payment therefor the bonds of the corporation. This is a conversion of bonds into stock, and is lawful and regular. *Lohman v. New York, &c. R. R. Co.*, 2 Sandf. Super. Ct. 39 (1848); *Reed v. Hayt*, 51 N. Y. Super. Ct. 121 (1884).

other manner, to effect an increase or reduction of the capital stock of a corporation.¹ It is a general rule, where the whole amount of the capital stock has been regularly issued, and the corporation becomes liable, either to issue certain certificates to a wronged party, or pay him damages; that the court, having no authority to direct such an issue, can only give judgment that the corporation pay damages.

In Massachusetts a later and better rule prevails to the effect that the corporation in such a case may be compelled to issue the stock, but in order to prevent an illegal overissue it must purchase an equal amount of shares in the market.² Where corporate officers enter into a contract to pay for services, or property, wholly or partially, in stock of the corporation, a court will not, after the whole amount of the stock has been issued, decree a specific performance of the contract, but the aggrieved party is remitted to his action for damages.³

§ 285. *Shareholders, not directors, should authorize the increase.*—An increase or reduction of the capital stock of a corporation is such a fundamental change in its affairs that although it has been duly authorized by act of the legislature or by the charter of incorporation, it cannot lawfully be effected merely by the act or assent of the board of directors,⁴ but must be au-

¹ "When a corporation has issued certificates of stock (which are valid and not void) to the full extent of all the shares, which by law and the constitution of the company it may issue, no court can order the issuance of other shares, because in that respect the powers of the corporation have been exhausted." *Smith v. North American Mining Co.*, 1 Nev. 423 (1865). *Williams v. Savage Manfg. Co.*, 3 Md. Chan. 418 (1851); *Mechanics' Bank v. New York, &c. R. R. Co.*, 13 N. Y. 599 (1856). In an action for the conversion of shares, the question of an increase or reduction not being involved, it was said that "To require a new issue of stock, might in cases like this, where shares have gone into the hands of innocent purchasers, involve an overissue of stock, which would be illegal." *Baker v. Wasson*, 59 Texas, 140 (1883); s. c. 53 Id. 150 (1880).

² This rule, with an equitable adjustment of the conflicting interests of all the parties, where an owner of stock was deprived of it by forgery, was established

by the Supreme Judicial Court of Massachusetts in the cases of *Machinists National Bank v. Field*, 126 Mass. 345 (1879). See also *Pratt v. Machinists National Bank*, 123 Id. 110, and *Boston, &c., R. R. Co. v. Richardson*, 185 Id. 473, each of the three cases growing out of the same transaction.

³ *Finley Shoe, &c., Co. v. Kurtz*, 34 Mich. 89 (1876). In this case the court say: Where the capital stock may be increased by vote of the stockholders, "it certainly could not be within the implied powers of any corporate officer to obligate the corporation to any such increase, and thus indirectly do what the law permits to be done only by the body of corporators, specially convened for the purpose." In actions against corporations for conversion of stock, the relief demanded is usually in the alternative, being either for an issue of a certificate of stock, or else damages in lieu thereof.

⁴ *Percy v. Millaudon*, 3 La. 568, 585 (1832); *Eidman v. Bowman*, 58 Ill. 444 (1871); *Finley Shoe, &c., Co. v. Kurtz*,

thorized by the shareholders at a corporate meeting.¹ Where, however, the directors have made the change, and the stockholders have acquiesced therein, they are as fully bound as though the increase or reduction had been expressly authorized at a corporate meeting. The shareholders' assent to the change may be shown as conclusively by their conduct and acquiescence as by a formal vote.² But whether the assent of the shareholders to the increase by the directors, be express, as by formal vote at a corporate meeting,³ or implied, as where there is a mere passive

34 Mich. 89 (1876); *Crandall v. Lincoln*, 52 Conn. 78, 99 (1884); *People v. Parker Vein Coal Co.*, 10 How. Pr. 543 (1854). See also *Railway Company v. Allerton*, 18 Wall. 233 (1873). In that case a shareholder of a city railway company obtained an injunction restraining the directors from increasing the capital stock. The company's charter provided that the capital might be increased "from time to time, at the pleasure of said company," and also that "all the corporate powers of said corporation shall be vested in and exercised by a board of directors, and such officers and agents as said board shall appoint." Mr. Justice Bradley, in construing this latter clause to refer merely to the ordinary business transactions of the company, held that to increase the capital stock was not among the powers and duties of the directors, and said: "We are satisfied that the decree must be affirmed on the broad ground, that a change so organic and fundamental as that of increasing the capital stock of a corporation beyond the limit fixed by the charter, cannot be made by the directors alone, unless expressly authorized thereto. The general power to perform all corporate acts refers to the ordinary business transactions of the corporation, and does not extend to a reconstruction of the body itself, or to an enlargement of its capital stock." See also *Constitution of Illinois*, 1870, Art. XI, § 13; also *Act of March 26, 1872, Illinois*.

¹ See the cases cited in the preceding note. *Green's Brice's Ultra Vires* (2d edition), 495; *Morawetz on Corp.* (2d edition), § 512; *Taylor on Corp.*, § 228. *Cf. City of Chicago v. Jones*, 60 Ill. 383 (1871); *Matter of Wheeler*, 2 Abb. Prac. (N. S.) 361 (1866); *People v. Twaddell*, 18 Hun, 427, 432 (1879); *State v. Merchant*, 37 Ohio St. 251 (1881).

² *Sewell's Case*, L. R. 3 Chan. 131 (1868); *Lane's Case*, 1 De G., J. & S. 504

(1863); *Payson v. Stoeve*, 2 Dill. 428 (1873). Although the act authorizing the increase required the assent of the stockholders, yet it has been held that "the requisite assent of the stockholders can be shown by their conduct and acquiescence, and need not necessarily be established by any formal vote or resolution," and moreover that a shareholder is bound by the acts and acquiescence of an agent, who, knowing of the irregular increase of the stock, continued to act for his principal as a stockholder. *Payson v. Stoeve*, *supra*. And an amendment of the charter which allows the directors instead of the shareholders to authorize an increase of the capital, is not such a fundamental change in the constitution of the corporation as will operate to release non-assenting shareholders from the obligation on their stock. *Payson v. Withers*, 5 Biss. 269 (1873); *Payson v. Stoeve*, *supra*. The power to increase the capital stock may be vested in the directors. *Sutherland v. Olcott*, 95 N. Y. 93 (1884), holding also that when the power to increase the stock is by the charter vested in the company to be exercised through the directors, subject only to the limitation that the business should require an increase, the directors are the judges of whether the business actually require it, and so long as they act in good faith in exercising the powers their determination is conclusive. Their resolution, that "the capital stock of this company be, and the same is, hereby increased to—" is sufficient to effect the increase.

³ Upon the power of the shareholders, by subsequent action at a corporate meeting, to ratify and validate irregular acts of the directors, when such acts were not fraudulent or in derogation of the rights of the corporation or its creditors, see *Supervisors v. Schenck*, 5 Wall. 772, 782 (1866); *Crump v. U. S. Mining Co.*, 7

assent or acquiescence on the part of the shareholders,¹ it is equally sufficient to validate the increase, provided the act of the directors be in other respects lawful.² But although the shareholders have regularly voted to increase the capital stock, in pursuance of adequate legislative authority, still, inasmuch as the increase is not accomplished until the shares are actually issued, the vote may be reconsidered in a lawful manner at any time before the stock is finally issued.³

§ 286. *Pre-emptive right of the old stockholders to buy the new stock.*—When the capital stock of a corporation is increased by the issue of new shares, each holder of the original stock has a right to offer to subscribe for and to demand from the corporation such a proportion of the new stock as the number of shares already owned by him bears to the whole number of shares before the increase. This pre-emptive right of the shareholder, in respect of new stock, is well recognized.⁴ But this applies only

Gratt. 352 (1851); *Arlington v. Peirce*, 122 Mass. 270 (1877); *Waldo v. Portland*, 33 Conn. 363 (1866); *Aurora Agricultural, &c., Society v. Paddock*, 80 Ill. 263 (1875); *McLoughlin v. Detroit, &c., R. Co.*, 8 Mich. 100 (1860); *Hayward v. Pilgrim Society*, 21 Pick. 270 (1838); *Bank of Columbia v. Patterson*, 7 Cranch, 299, 307 (1813). *Cf.* *Twin Lick Oil Co. v. Marbury*, 91 U. S. 587 (1875); *Hotel Company v. Wade*, 97 Id. 13 (1877); *Pneumatic Gas Co. v. Berry*, 113 Id. 322 (1884); *Union Pacific R. Co. v. Credit Mobilier*, 135 Mass. 367 (1883); *United States Rolling Stock Co. v. Atlantic, &c., R. R. Co.*, 34 Ohio St. 450 (1878); *Peterson v. The Mayor*, 17 N. Y. 449 (1858); *Reed v. Hayt*, 51 N. Y. Super. Ct. 121 (1884); *Buell v. Buckingham*, 16 Iowa, 284, 295 (1864).

¹ To the point that a passive assent is such an acquiescence as will avail to bind a principal and make a shareholder liable for the irregular acts of the directors, if they are not fraudulent or in violation of law, see *Gold Mining Co. v. National Bank*, 96 U. S. 640 (1877); *Mining Co. v. Anglo Californian Bank*, 104 Id. 192 (1881); *s. o. sub nom.* *Anglo Californian Bank v. Mahoney Mining Co.*, 5 Sawyer, 255 (1878); *Bank of Pennsylvania v. Reed, 1 Watts & S.* 101 (1841); *Hilliard v. Goold*, 34 N. H. 230 (1856); *Pacific R. Co. v. Thomas*, 19 Kan. 256 (1877); *Chicago Building Society v. Crowell*, 65 Ill. 453 (1872); *Darst v. Gale*, 83 Id. 136

(1876); *Bleu v. Bear River, &c., Mining Co.*, 20 Cal. 602 (1862); *Perry v. Simpson, &c., Manfg. Co.*, 37 Conn. 520 (1871); *Bennett v. Maryland Fire Insurance Co.*, 14 Blatchf. 422 (1878); *Walworth Co. Bank v. Farmers Loan & Trust Co.*, 16 Wis. 629 (1863); *Chicago, &c., R. R. Co. v. James*, 24 Id. 388 (1869); *Phillips v. Campbell*, 43 N. Y. 271 (1870); *New Hope & Delaware Bridge Co. v. The Phenix Bank*, 3 N. Y. 156 (1849). *Cf.* *Terry v. Eagle Lock Co.*, 47 Conn. 141 (1879).

² An allegation of ratification must not be in general terms, but must set out specifically the facts constituting the ratification. *Eidman v. Bowman*, 53 Ill. 444.

³ *Terry v. Eagle Lock Co.*, 47 Conn. 141 (1879). In this case the court say: "It cannot be said that the capital is actually increased until the new stock is subscribed for at least. Until then there is an element of uncertainty about it. It may never be taken. It is very clear that the note to increase is not *per se* an increase."

⁴ *Gray v. Portland Bank*, 3 Mass. 364 (1807); *Eidman v. Bowman*, 53 Ill. 444 (1871); *Reese v. Bank of Montgomery*, 31 Penn. St. 78 (1855); *Re Wheeler*, 2 Abb. Prac. (N. S.) 364 (1866); *Miller v. Illinois, &c., R. R. Co.*, 24 Barb. 312 (1857); *Jones v. Morrison*, 31 Minn. 140 (1883); *Bank of Montgomery v. Reese*, 26 Penn. St. 143 (1856). *Cf.* *Curry v. Scott*,

when the capital is actually increased, and not to a reissue of any portion of the original stock.¹ The right must be exercised within a fixed or a reasonable time, and if the shareholder fails to avail himself of it, he is barred by laches or acquiescence, of his right to contest a disposition of the stock to some one else.² The corporation cannot compel the old stockholders, upon their subscription for new stock, to pay more than the par value therefor. They are entitled to it without extra burden or expense, beyond the regular subscription price.³ In the absence of laches or acquiescence on the part of the shareholder, an attempt to deprive him of this right will be enjoined.⁴ When the newly issued

54 Penn. St. 270 (1867); *Wilson v. Bank of Montgomery County*, 29 Id. 537 (1857); *Mason v. Davol Mills*, 132 Mass. 76 (1882); *Pratt v. American Bell Tel. Co.*, 12 Am. & Eng. Corp. Cas. 110 (Mass. 1886); *Ohio Insurance Company v. Nunnemacher*, 15 Ind. 294 (1860). In *Reese v. Bank of Montgomery*, 31 Penn. St. 78 (1855), the Supreme Court of Pennsylvania, in an action for damages against the corporation for refusal to allow a subscription for new shares, in violation of a shareholder's preemptive right, says: "Since the acts of incorporation do not declare how the untaken stock shall be disposed of, it stood like all the other corporate franchises and belonged to the corporators, and they had a right to all the profits that could be derived from it . . . the bank held the right in trust for its members. The directors might order it sold, and then the profits would be shared among the members at the next dividend, or they might allow each member to subscribe for his proportion of the new stock as nearly as it could be fixed in integral shares." In *Jones v. Morrison*, 31 Minn. 140 (1883), the court says: "When new stock is issued each share of it has an interest in the surplus equal to that pertaining to each share of the original stock. And if the corporation, either through the officers, directors, or majority of stockholders, may dispose of the new stock to whomsoever it will, at whatever price it may fix, then it has the power to diminish the value of each share of old stock, by letting in other parties to an equal interest in the surplus, and in the good-will or value of the established business." This case holds that such also may be the rule by contract where unissued shares of the original capital stock is paid for by profits and issued to

one stockholder in trust for all. The corporation cannot then sell it for the benefit of the corporation. In Massachusetts this right is preserved in the statutes, Chap. 106, § 37; chap. 112, § 58. In New York, in banking corporations, it is secured to the shareholder by statute. Session Laws 1878, chap. 274, § 5. But the pledgee of stock who holds it merely as collateral security, is not entitled to this right to take up new shares. The right belongs to the pledgor. *Miller v. Illinois Central R. R. Co.*, 24 Barb. 812 (1857).

¹ *State v. Smith*, 48 Vt. 266; *Hartbridge v. Rockwell*, R. M. Charlton (Ga.), 260 (1828). In *State v. Smith*, *supra*, the court, by Redfield, J., said: "When new stock is issued that shares equally with the existing stock, the shareholders have a right that it shall be so distributed as not to divest any stockholder of his present vested right in property; and the proportionate share of the accumulated profits is represented by the shares and in vested property, as much so as the shares themselves. . . . But this was not a new issue of stock, but a portion of the original subscription. . . . The transfer of the stock to the corporation suspends the right to vote upon it, and may be a merger if so understood by the parties. The right of the directors to reissue or sell such stock for honest purposes and for the benefit of the corporation, is reasonable and amply sustained by the authorities."

² *Terry v. Eagle Lock Co.*, 47 Conn. 141 (1879); *Hart v. St. Charles St. R. R. Co.*, 30 La. Ann. 758 (1878); *Brown v. Florida Southern Ry. Co.*, 19 Fla. 472 (1882).

³ *Cunningham's Appeal*, 108 Penn. St. 546 (1885).

⁴ A stockholder's remedy, it is said,

shares have all been distributed, or sold to others, in violation of a shareholder's pre-emptive right, his only remedy is an action at law against the corporation for damages. And the measure of damages has been declared to be the excess of the market value above the par value at the time of the issue of the shares, with legal interest on such excess.¹

A mere verbal notice by the stockholder to the corporation, that he will take his proportion of the new issue under an increase, is held in Louisiana to be sufficient to render the company liable in damages for selling the shares to some one else. This amounts to a regular offer to subscribe for the shares, and when a tender of payment is made in the usual manner, the shareholder, who has made such an offer, can be put in default only by a tender of the certificate and demand of payment by the corporation.² The corporation may, however, and usually does, limit the time within which the shareholders may signify their intention to take up the new

in such a case, is clearly against the corporation, and he is not obliged to sue at law for damages. "The effect of such an action [*i. e.*, the action for damages] would be to convert part of his interest as a shareholder into a judgment for damages; in other words to sell a portion of his stock to the corporation. . . . The judgment to be effectual must be against the corporation itself, not against the directors personally, who may be changed from time to time." *Dousman v. Wisconsin & Lake Superior Mining & Smelting Co.*, 40 Wis. 418 (1876). In this case it is also held that the shareholder, where the stock is not yet fully issued, may have a decree in a court of equity restraining the whole issue, or else that there be an equitable distribution, and if the shares are already partially distributed that the proper amount be issued to the party complainant. *Of. Eidman v. Bowman*, 58 Ill. 444. In Massachusetts, however, where the courts formerly possessed but a limited equity jurisdiction, this is not the rule, and in that State it is held that there is no power in the courts, acting as courts of chancery, to decree a specific performance in favor of the shareholder, who alleges that shares which ought to have been allotted to him have been wrongfully sold or issued to others; or in other words, that the courts have no power to compel the corporation or the directors to issue the shares to the

party aggrieved. *Sewall v. Eastern R. R. Co.*, 9 Cush. 5 (1851). But an action will lie against the corporation for damage. *Gray v. Portland Bank*, 3 Mass. 364 (1807).

¹ *Eidman v. Bowman*, 58 Ill. 444; *Reese v. Bank of Montgomery*, 31 Penn. St. 78 (1855); *Gray v. Portland Bank*, 3 Mass. 364 (1807). In *Eidman v. Bowman*, *supra*, it is said that: "When the company determine to increase their capital stock, within the limits of their charter, each of the previous stockholders has the right to a proportionate number of the new shares, or a proportionate amount of the new stock, if it should be added to the old shares. If he be deprived of it he may sue the company by a special count in assumpsit, and recover for the loss, and it has been held that the measure of damages is the excess of the market value of the stock above the par value at the time of payment of the last installment, with interest on the excess. . . . It would be a dangerous power to intrust to directors to increase the stock of the company at pleasure, and to sell it to whom they choose. . . . The power is such that we will not infer its existence in a charter unless clearly expressed."

² *Hart v. St. Charles St. Ry. Co.*, 30 La. Ann. 758 (1878). In such a case no special formalities of subscription are necessary to secure the shares.

shares, and may require a part payment within that time upon the shares.¹ The stockholder, therefore, who brings his action against the corporation for damages, for refusal to allow him to subscribe for the new shares, or for selling the shares to some one else, or for depriving him in any other way of them, must allege and prove that he demanded the shares and offered to subscribe and pay for them in the regular way, within the time fixed for such subscriptions.² Other shareholders similarly aggrieved are not to be joined as parties complainant. Each stockholder sues alone, inasmuch as the liability of the corporation in these cases is several and not joint.³

§ 287. *Issue of new stock by a stock dividend.*—A frequent method of issuing an increase of the capital stock is by a stock dividend. In England there is some doubt as to whether such

¹ Sewall v. Eastern R. R. Co., 9 Cush. 5 (1851); Hart v. St. Charles St. Ry. Co., 30 La. Ann. 758 (1878).

² Wilson v. Bank of Montgomery County, 29 Penn. St. 537 (1857).

³ Dousman v. Wisconsin & Lake Superior Mining and Smelting Co., 40 Wis. 418 (1876). In Williams v. Savage Manufacturing Co., 3 Md. Chan. 418, 430, it is also held, that ordinarily a shareholder suing the corporation "stands before the court precisely in the attitude of an ordinary suitor, and, upon his application to compel the production of books and papers from the adversary, must show himself entitled upon the general practice and law regulating the subject." And further, that the court will not, upon such an application, order the books of a corporation to be brought into court, unless the party asking the order "should, with a reasonable degree of certainty, designate the books and papers required, and the facts expected to be proved by them." In an early Indiana decision it is said to be the law that where, in the charter, directors are given full power to effect an increase of the capital stock, "on such terms and conditions and in such manner as to them shall seem best," they may authorize the increase without the consent of the shareholders; that as to each increase there is no pre-emptive right, and that accordingly the newly issued shares may be disposed of as the directors determine. Ohio Insurance Co. v. Nunnemacher, 15 Ind. 294 (1860). Cf. Great Falls, &c., R. R. Co. v. Copp, 38 N. H.

124 (1859). So also in New York, it is said that the executory purchaser of shares of the original stock is not entitled to the proportionate amount of new stock on an increase of the capital. Miller v. Illinois Central R. R. Co., 24 Barb. 312 (1857). So also it seems in Massachusetts, Pratt v. American Bell Telephone Co., 5 Northeastern Rep. 307 (1886), an important application of this general doctrine of the shareholder's pre-emptive right, to take new shares, is the rule that, where upon the organization of the company only part of the authorized capital stock is issued, the right to take the remainder, whenever it shall be issued, vests in the original shareholders, in proportion to the amount of the stock first issued which they severally own. Eidman v. Bowman, 58 Ill. 444; Gray v. Portland R. R. Co., 3 Mass. 364 (1807). Angell & Ames on Corp. (11th edition), §§ 554, 555. This is denied in Pennsylvania, where the courts have taken decided ground that, in such a case, there is no prior or superior right in the original shareholder as to the remainder of the capital. "It is not to be admitted," say the court in Curry v. Scott, 24 Penn. St. 27 (1867), in discussing this question, "that an old stockholder had a right to subscribe to the untaken stock, superior to the right of one who owned no stock. If this were so a first subscriber might compel all the remaining untaken stock to be sold, or at least would have a right to exclude any other person from subscribing."

dividends may be imposed upon stockholders who object to them and demand the money dividend in lieu of which the stock is issued.¹ In this country such dividends are legal unless prohibited by constitutional or statutory provisions.² But in all cases of a stock dividend, as a method of issuing an increase of the capital stock, there must be in the possession of the corporation an amount of property over and above its corporate debts, equal to the whole capital stock, including the increase, and this amount cannot afterwards be used for any kind of a dividend.

§ 288. *Liability of the shareholder upon an increase of the capital stock.*—A person subscribing for shares of stock upon an increase of the capital stock is liable thereon, the same as a subscriber, to the original capital stock. In some respects, he cannot set up defenses that an original subscriber might have set up. Thus, a subscriber for increased stock cannot defeat an action to enforce his subscription by setting up the failure of the corporation to obtain subscriptions for the whole of the authorized increase.³ In general, a subscriber to an increase of stock cannot interpose defenses to his subscription, which subscribers to the original stock could not have raised, such, for an example, as technical objections to the validity of his contract of subscription.⁴ Nor can the subscriber set up that the increase was unauthorized and illegal. It is for the State alone to raise the question whether corporate capital stock has been lawfully and regularly increased.⁵ Especially is it the rule that, as against corporate creditors, stockholders who have subscribed for the increased stock, accepted the certificate, and received dividends thereon, are estopped from set-

¹ See Chapter on Dividends.

² *Id.*; also § 51, *supra*. "If the corporation have the power to increase the capital stock, the manner of effecting the increase not being prescribed in the enabling act, it is immaterial whether such increase is made by awarding the stock to stockholders, as dividends in lieu of money, retaining the money for the purpose of the company, or by paying the stockholder the dividends in cash from the earnings of the company, and selling the stock in the market to raise money for the use of the corporation." *Howell v. Chicago, &c., R. R. Co.*, 51 Barb. 378 (1868). In this case it seems to be held that a statement of the board of directors, in their report, that no more stock is to

be issued, will not prevent such issue, and that the increase of the stock of a foreign corporation will not be inquired into by the court of another State. *Cf. Reese v. Bank of Montgomery*, 31 Penn. St. 78 (1855). An increase of the capital stock, by the issue of new shares and the sale of them for less than their par value, is not such an "issue of fictitious stock" as the California State Constitution forbids. Art. XII, § 11; *Stein v. Howard*, 65 Cal. 616 (1884).

³ *Clarke v. Thomas*, 34 Ohio St. 46 (1877); *Nutter v. Lexington, &c. R. R. Co.*, 6 Gray, 85 (1856).

⁴ *Kansas City Hotel Co. v. Hunt*, 57 Mo. 126 (1874).

⁵ *Pullman v. Upton*, 96 U.S. 328 (1877).

ting up that the stock was increased in an irregular or unlawful manner.¹ Stockholders of the original capital stock are of course not liable for the defaults of subscribers to the increased capital stock.²

§ 289. *Rights and liabilities of the shareholders upon a reduction of the capital stock.*—Upon an authorized reduction of the capital stock of an incorporated company, regularly effected, the amount of corporate assets, over and above the amount of the capital stock as reduced, is equivalent to surplus profits, and may be treated as such by the corporation. It may be set aside as surplus, or it may be divided among the shareholders proportionally by a dividend, subject, however, in all cases, to the rights of

¹ Chubb v. Upton, 95 U. S. 665 (1877); Sheldon Hat Blocking Co. v. Eickemeyer, &c. Co., 90 N. Y. 607, 612 (1882); Kent v. Quicksilver Mining Co., 78 N. Y. 159, 187 (1879); *In re Miller's Dale, &c. Co.*, L. R. 31 Ch. D. 211 (1886); Aspinwall v. Sacchi, 57 N. Y. 331 (1874); Buffalo, &c. R. R. Co. v. Cary, 26 N. Y. 75 (1862); Eaton v. Aspinwall, 19 N. Y. 119 (1859); Veeder v. Mudgett, 95 N. Y. 295 (1884)—the last case holding that a statute allowing increase to be made by stockholders in meeting assembled on a specified notice, is invalid if the notice did not conform to the statute, but that the stockholders are liable nevertheless to corporate creditors on such stock. To the general point that a subscriber or shareholder, as against creditors, will be estopped from questioning the formal regularity or validity of corporate acts, by acquiescence or assent, or by receiving benefit under such acts, or by allowing other persons to give the corporation credit upon the faith of those acts, see Dutchess Collar Manfg. Co. v. Davis, 14 Johns. 237 (1817); Bissell v. Michigan Southern R. R. Co., 22 N. Y. 253 (1860); Methodist Episcopal Union Church v. Pickett, 19 N. Y. 482 (1859); Upton v. Hansbrough, 3 Biss. 417; Ogilvie v. Knox Insurance Co., 22 How. 380 (1859); Rensselaer, &c. Plankroad Co. v. Westel, 21 Barb. 56 (1855); Thompson on Liability of Stockholders, §§ 160-175, 407, 410, 414; Morawetz on Corporations (2d edition), §§ 761-767; Herman on Estoppel (2d edition), §§ 1178, 1248). Cf. Granger's Life, &c. Ins. Co. v. Kamper, 73 Ala. 325 (1882); Kansas City Hotel Co. v. Harris, 51 Mo. 464

(1873), and see McCarthy v. Lavasche, 89 Ill. 270 (1878). Lindley, in his learned work, says: "If shares can, under any circumstances legally exist, then, however improper their issue may have been, the company and the holder of them may be estopped from denying their existence, and the holding of them by him. But if they cannot legally exist, the person taking them cannot, by estoppel or otherwise, become a member in respect of them." 1 Lindley on Partnership (4th ed.), 134; see also vol. 2, p. 1349, citing Campbell's Case, L. R. 9 Chan. 1 (1873); Challis' Case, L. R. 6 Chan. 266 (1871); Hare's Case, L. R. 4 Chan. 503 (1869); Bank of Hindustan v. Alison, L. R. 6 C. P. 54, 222 (1870); Stace & Worth's Case, L. R. 4 Chan. 682 (1869); Smith's Case, Id. 611 (1869); Spackman v. Evans, L. R. 3 H. L. 171 (1868). But Morawetz well says: "This statement of the law, however, is hardly sustained by the authorities cited by the learned author." Morawetz on Corp. (2d edition), § 766.

² Thus where the statute, as in New York, Laws of 1848, chap. 40, §§ 10, 20, 21, 22, makes stockholders liable to creditors until the capital stock is fully paid in, that liability is terminated when such full payment has been made, and the proper certificate to that effect duly made and recorded; and a subsequent increase of the capital stock will not render the old shareholders liable to creditors until that increase is likewise fully paid in and regularly certified. The liability of the old stockholders once terminated cannot be revived. Veeder v. Mudgett, 95 N. Y. 295 (1884).

previous corporate creditors.¹ But it is not the rule that the reduction of the capital stock of a corporation always authorizes the distribution among the stockholders of a sum equal to the difference between the original and the reduced amount of capital. Such a distribution is lawful only when it appears that the original capital stock is unimpaired. The corporation can divide among its stockholders only such a sum as will leave with the corporation an amount equal to the reduced capital stock.² Not only this, but corporate creditors who were such before the reduction, may disregard the reduction and enforce payment of their debts from the original unpaid subscriptions, as though no reduction had taken place.³ But creditors whose debts were contracted subsequently to the reduction, can look only to the capital stock as reduced, for security. They will be held to have given the credit upon the faith of that amount of stock alone.⁴

§ 290. *Change in the number or par value of the shares.*—It is a principle of law closely related to those already set forth in this chapter, and well settled, that the number of shares

¹ *Strong v. Brooklyn Crosstown R. R. Co.*, 93 N. Y. 426 (1883); *Seeley v. New York National Exchange Bank of New York*, 8 Daly, 400 (1878); s. c. aff'd, 78 N. Y. 608 (1879). In the case last cited, where a national bank had reduced its capital stock as authorized by statute, (U. S. Rev. Stat. § 5143) the court say: "If instead of surrendering all its corporate powers, a corporation, by reducing its capital stock, relinquishes a portion of them, it seems to me that the shareholders may properly claim a distribution of the money which the corporate body has no longer the right to use as capital. . . . The return of the reduced capital to the shareholders is not a subject for the exercise of a director's discretion." The shareholder may, it was decided, sue for his share and recover it. The case of *Strong v. Brooklyn Crosstown R. R. Co.*, *supra*, holds that a reduction of the capital stock does not authorize the distribution among the stockholders of a sum equal to the difference between the amount originally named as the capital, and the reduced amount fixed by the vote of the stockholders, even if it appears that the original amount was actually paid in. To authorize such a distribution, if the original capital has been paid in, it should appear that the capital so

paid in has not been impaired, and if it has been impaired it should appear that the corporation still has on hand actual capital, available for the payment of debts, exceeding the amount to which it has reduced its capital, and if it has, the excess only ought to be distributed." But "the excess of its funds or property actually on hand, over and above the sum which the company is bound to keep as capital (viz. its nominal capital, as reduced), is reduced into a surplus fund which it can dispose of by dividing it among its stockholders." This excess is to be determined by an actual inventory of its assets.

² *Strong v. Brooklyn Crosstown R. R. Co.*, 93 N. Y. 426 (1883).

³ *In re State Insurance Co.*, 11 Biss. 301 (1882); s. c. 14 Fed. Rep. 28; *Bedford R. R. Co. v. Bowser*, 48 Penn. St. 29 (1864). Shareholders have no power to avoid liability on their stock by reducing either the amount of it or the par value of the shares. *Dane v. Young*, 61 Me. 160 (1872). *Cf. Bedford R. R. Co. v. Bowser*, 48 Penn. St. 29 (1864).

⁴ *Hepburn v. Exchange, &c. Co.*, 4 La. Ann. 87 (1849); *Palfrey v. Paulding*, 7 Id. 363 (1852); *Cooper v. Frederick*, 9 Ala. 742 (1846). *Cf. In re State Ins. Co.*, 14 Fed. Rep. 28 (1882); s. c. 11 Biss. 301.

into which the capital stock has been divided, and the par value of those shares, can neither be increased nor diminished, in number or in value, without express warrant of authority either from the legislature or the charter of the company.¹ When the charter does not fix the number or amount of the shares, it devolves upon the shareholders or directors to fix them, and in such a case it seems that the limit established might lawfully be changed without special authority.²

§ 291. *Unauthorized increase of stock may amount to overissued stock.*—Where the full capital stock of a corporation has been issued, and there is no statute or charter provision authorizing an increase of the stock, it is clear that any issue of stock in excess of the capital stock is not a legitimate increase of the capital stock. It is unauthorized and illegal, and is termed in law an overissue of stock. There is a clear distinction between overissued stock and an irregular increase of stock. The former exists when it is made, although no increase of the stock is authorized by the charter or by statute. The latter occurs when there is a statutory or charter provision authorizing an increase of the stock, but the formalities prescribed for making that increase have not been strictly complied with. Overissued stock is void while an irregular increase of stock is merely voidable.

§ 292. *Overissued stock is absolutely void.*—By overissued stock is to be understood stock issued in excess of the amount limited and prescribed by the act of incorporation. Certificates of stock issued in excess of the certificates that represent the full, authorized capital stock of the corporation, represent overissued stock. Such stock is spurious and wholly void. This is the set-

¹ *Salem Mill-Dam Corporation v. Ropes*, 6 Pick. 23 (1827); *Knowlton v. Congress, &c. Spring Co.*, 14 Blatchf. 364 (1877); *Grangers Life, &c. Ins. Co. v. Kamper*, 73 Ala. 325 (1882); *Re Financial Corporation* (Holmes Case), L. R. 2 Chan. 714, 733 (1867); *Droitwich Salt Co. v. Curzon*, L. R. 3 Eq. 42; *Smith v. Goldsworthy*, 4 Q. B. 430 (1843); *Sewell's Case*, L. R. 3 Chan. 131 (1868). "A corporation, with a fixed capital, divided into a fixed number of shares, can have no power of its own volition, or by any act of its officers and agents, to enlarge its capital or increase the number of

shares into which it is divided. The supreme legislative power of the State can alone confer that authority." It cannot be increased "by the covert or fraudulent efforts of one or more of the agents of the corporation." *N. Y. & New Haven R. R. Co. v. Schuyler*, 34 N. Y. 80, 48 (1865). *Cf. Scovill v. Thayer*, 105 U. S. 143 (1881); *Morawetz on Corporations* (2d edition), § 434. In New York a statute allowing such a change exists. *New York Session Laws*, 1866, chap. 73.

² *Somerset, &c. R. R. Co. v. Cushing*, 45 Me. 524 (1858).

tled law, and it prevails equally whether the overissue is the result of accident, or mistake, or want of knowledge of the law, or is due to fraud and intentional wrongdoing. The *animus* or intent of the parties to the overissue is not material. Over-issued stock, no matter how overissued, represents nothing, and is wholly and entirely valueless and void. So rigid and well established is this rule, that not even a *bona fide* holder of such stock can give to it any validity or vitality. It is void.¹

¹ The great and leading case on this subject is *New York, &c., R. R. Co. v. Schuyler*, 34 N. Y. 30 (1865). *Cf. Mechanics' Bank v. New York, &c., R. R. Co.*, 13 Id. 599 (1856). In the litigation growing out of these cases it appeared that many thousands of shares of the stock of the New York & New Haven R. R. Co. had been fraudulently issued by the transfer agent, Robert Schuyler, in excess of the amount of stock limited by the charter, and that much of such overissued stocks was in the hands of *bona fide* holders. In the case of the *Mechanics' Bank v. New York, &c., R. R. Co.*, 13 N. Y. 599 (1856), it was decided that the spurious certificates of stock issued by Schuyler were void, upon the ground of a want of corporate power to create shares of stock in excess of the prescribed amount; that a bank, having taken such spurious shares as collateral security for a loan, did not thereby acquire a right, legal or equitable, to any stock, and that the railroad company was not responsible to the bank for damages sustained by it through dealing upon the faith of the certificate. The court said that the capital stock cannot be increased by any acts of the agents of the company. Certificates, when issued for shares of stock in excess of the capital stock, have not the effect of increasing the capital stock. Subsequently the railroad company, being threatened with more than one hundred suits by holders of the over-issued stock, brought an action in equity against Schuyler and 320 other defendants—*New York, &c., R. R. Co. v. Schuyler et al.*, 34 N. Y. 30 (1865)—to have the fraudulent certificates and transfers made by Schuyler and held by the other defendants adjudged to be spurious and void, to have them brought into court and cancelled, and to enjoin the defendants from further prosecuting certain actions then pending, and from commencing other suits against the company, to enforce such certificates and transfers, or to recover

damages for any reason connected with them. This case is one of the landmarks of the law. The doctrine of the earlier case of the *Mechanics' Bank v. New York, &c., R. R. Co.*, 13 N. Y. 599 (1856), that overissued stock is void, is vigorously sustained. In answering the question whether the stock purporting to be created by the false certificates and fraudulent transfers of Schuyler could be valid stock of the corporation and become part of its capital, the court said: "In the nature of things this is impossible. A corporation with a fixed capital divided into a fixed number of shares, can have no power of its own volition, or by any act of its officers and agents, to enlarge its capital, or increase the number of shares into which it is divided. The supreme legislative power of the State can alone confer that authority, and remove, or consent to the removal of restrictions which are part of the fundamental law of the corporate being, and hence every attempt of the corporation to exert such a power, before it is conferred, by any direct and express action of its officers, is void, and hence every indirect and fraudulent attempt to do so is void, for, if such a result cannot be accomplished directly, by the whole machinery of the corporate powers, it is absurd to suppose that it can be produced by the covert or fraudulent efforts of one or more of the agents of the corporation. The special term was therefore right in holding that the spurious stock attempted to be created by Schuyler in excess of the capital, formed no part of the capital stock of the company, but was utterly invalid, and it necessarily followed . . . that the plaintiffs were entitled to have all certificates and transfers which represented such spurious stock declared void and ordered to be cancelled." See also, as to the point that overissued stock is void even in the hands of *bona fide* holders, *People's Bank v. Kurtz*, 99 Penn. St. 344 (1882); *Bruff*

Overissued or spurious stock may, however, it seems, be legalized by a subsequent legal increase of the capital stock.¹

§ 293. *Liability of the corporation as to overissued stock.*—Although it is settled law that overissued stock is void and valueless, and that no action lies on the certificate either to compel the corporation to recognize the holder as a stockholder, or to issue in place thereof a valid certificate, yet where overissued certificates of stock, signed or purporting to be signed by the corporate officers having the authority to issue stock, and actually issued by such officers, are purchased by any person, or are taken in any manner in good faith and for value, such *bona fide* holder may sue the corporation in tort, and recover damages.²

The cases to this point proceed upon the theory that a corporation, like a natural person, is liable in damages for the torts and frauds of its agents when acting within the scope of their proper employment, and that, when fraudulent certificates are issued by its officers, and pass innocently into the hands of *bona fide* holders for value, the corporation is estopped to deny the authority of such agents, and cannot escape liability for damages so resulting.

If an innocent holder of overissued stock brings an action in equity to compel the corporation to record the transfer, he will be denied that relief, but may have, in lieu thereof, damages at law.³ The better remedy in such a case, therefore, is an action at law, and the measure of damages is the market value of the stock at the time the transfer was demanded.⁴

v. Mali, 36 N. Y. 200 (1867); *People v. Parker, &c., Co.*, 10 How. Prac. 543 (1854); *Sewell's Case*, L. R. 3 Chan. Ap. 131, 138 (1868); *Wright's Appeal*, 99 Penn. St. 425 (1882); *Scovill v. Thayer*, 105 U. S. 143 (1881).

¹ *Sewell's Case*, L. R. 3 Chan. Ap. 131 (1868); *New York, &c., R. R. Co. v. Schuyler*, 54 N. Y. 30, 56, 57 (1865).

² *New York, &c., R. R. Co. v. Schuyler*, 54 N. Y. 30, 49, 60 (1865); *Bruff v. Mali*, 36 Id. 200 (1867); *Titus v. Great, &c., Road Co.*, 5 Lans. 250 (1872); s. c. 61 N. Y. 237 (1874); *Bank of Kentucky v. Schuylkill Bank*, Parsons' Select Cas. 180 (1846); *Tome's Parkersburg, &c., R. R. Co.*, 39 Md. 36 (1873); *Western, &c., R. R. Co. v. Franklin Bank*, 60 Id. 36 (1882); *Willis v. Phila., &c., R. R. Co.*, 6 Week. Notes Cas. 461 (1879); *Willis v. Fry*, 13 Phila. 33 (1879); *People's Bank*

v. Kurtz, 99 Penn. St. 344 (1882). See also *Daly v. Thompson*, 10 Mee. & W. 309 (1842). *In re Bahia, &c.*, R. R. Co., L. R. 3 Q. B. 584, 595 (1868); *Simm v. Anglo, &c., Co.*, L. R. 5 Q. B. Div. 188 (1879); *Waterhouse v. London, &c., R. R. Co.*, 41 L. T. (N. S.) 553 (1879); *Mandelbaum v. North, &c., R. R. Co.*, 4 Mich. 465 (1857); *Wright's Appeal*, 99 Penn. St. 425 (1882).

³ *Willis v. Phila., &c., R. R. Co.*, 6 Week. Notes Cas. 461 (1879); *People's Bank v. Kurtz*, 99 Penn. St. 344 (1882).

⁴ *People's Bank v. Kurtz*, 99 Penn. St. 344 (1882); *Willis v. Phila., &c., R. R. Co.*, 6 Week. Notes Cas. 461 (1879); *People v. Parkersburg, &c., R. R. Co.*, 39 Md. 36 (1873). It is however a condition precedent to maintaining such an action that the holder of the overissued stock discharge any lien upon it which would have properly attached to genuine stock under

§ 294. *Defenses of the corporation to such actions.*—It frequently happens that an overissue of stock is made without a strict compliance with the formalities of an issue of genuine stock. Generally, certificates of stock must, according to the by-laws of the corporation, be signed by certain specified corporate officers. Often, however, nothing in the charter or by-laws of the corporation regulates the form or contents of a certificate of stock. Accordingly, when action is brought against a corporation on overissued stock, the defense is some times set up that the certificates were not signed by the proper officers, or were not issued with the usual formalities, and consequently that, the purchaser having had notice of the infirmity, the corporation is not liable. But such a defense is not favored by the courts.¹ But where the charter provided that certificates of stock should be signed by the president, directors, and treasurer, fraudulent overissues signed by the president and treasurer alone, were held not sufficient to charge the corporation.²

§ 295. *Personal liability of the officers of the corporation on overissued stock.*—The officers of a corporation, who are authorized to issue certificates of stock to the stockholders, are liable, in tort, both to the immediate purchasers from them of spurious stock, falsely and fraudulently certified by them, and also to any subsequent purchaser buying upon the faith of the false certificate, and sustaining damage thereby.³ There may

the same conditions. *Mt. Holly Paper Co.'s Appeal*, 99 Penn. St. 513 (1882).

¹ *New York, &c., R. R. Co. v. Schuyler*, 34 N. Y. 30 (1865). Thus, where an officer of a corporation fraudulently issued stock for his own use, controlled all the books relating to the stock, and countersigned all the certificates, the corporation was held liable for the spurious stock. *Tome v. Parkersburg, &c., R. R. Co.*, 39 Md. 36 (1873). So also where overissued stock is issued under the genuine seal of the corporation, the corporation is liable. *People's Bank v. Kurtz*, 99 Penn. St. 344 (1882). See also *Manhattan Beach Co. v. Harned*, 27 Fed. Rep. 484 (1886). The last case, however, was where the corporate officers issued stock, not in excess of the capital stock, but a part of the unissued original capital stock. They issued it not for the corporation, but in fraud of it and for their own benefit.

This class of cases is treated of in Chapter XXI, under the head of Forgery.

² *Holbrook v. Fauquier, &c., Turnpike Co.*, 3 Cranch C. C. 425 (1829). And overissued stock issued by the president to his private debtor, in payment of his private debt, has been held not to confer on such debtor a right to hold the corporation responsible. *Wright's Appeal*, 99 Penn. St. 425 (1882). In this case the court assumes that the debtor could not be heard to claim *bona fides*.

³ *Bruff v. Mali*, 36 N. Y. 200 (1867); *Seizer v. Mali*, 41 Id. 619 (1869); reversing s. c. 32 Barb. 76 (1860); 11 Abb. Prac. 129; *Cazeaux v. Mali*, 25 Barb. 578 (1857); *Shotwell v. Mali*, 38 Id. 445 (1862). A person receiving stock from the directors of a corporation, in pledge for a loan to it, they knowing that the stock was overissued, may sue the directors for damages in an action for deceit.

be either a joint action against the corporation and the corporate agents issuing the stock, or a separate action against either.¹ In actions against the directors for frauds in the overissue of stock, the corporation is a party.²

§ 296. *Liability of the vendor of overissued stock.*—In the absence of fraud, the purchaser of overissued and spurious stock cannot hold his vendor liable thereon. The *bona fide* vendor can be held to warrant only his own title to the shares, not the right of the corporation to issue them. If he came by them honestly and sells them in good faith, there is no recourse to him, even though they turn out to be spurious.³ When, however, the vendor is guilty of fraud in the transaction he is liable.⁴

§ 297. *Equity will enjoin voting, transferring, or dividends on such stock, and will adjust the rights of all parties.*—A court of equity will, upon a proper application, grant an injunction to prevent the transfer of illegally issued stock, or the payment of dividends thereon, or the voting of the pretended owners of such stocks.⁵ The most effectual remedy in these cases is a suit in equity, instituted by the corporation whereby, in one proceeding, the rights and liabilities of all persons concerned

Whitehaven, &c., Co. v. Reed, 54 L. T. Rep. 360 (1886); Natl. Exchange Bk. v. Sibley, 71 Ga. 726 (1883).

¹ Bruff v. Mali, 36 N. Y. 200 (1867). And when the action is against the officers responsible for the fraudulent overissue, if the evidence shows that the entire capital stock of the company had been issued prior to the dates of the certificates purchased or held by the plaintiff, and if it appears that the defendants prior thereto, had, as officers of the corporation, issued spurious certificates of stock, then there is a presumption of law, that the certificates in controversy are false and fraudulent, and the burden is upon the defendants to show that these particular certificates were issued, either upon the surrender of certificates of genuine stock, or upon the transfer on the books of the company of such stock, facts peculiarly within the knowledge of the corporate officers. Shotwell v. Mali, 38 Barb. 445, 469 (1862), a well-considered case; Bruff v. Mali, 36 N. Y. 200 (1867).

² Venezuela, R. R. Co. v. Kisch, L. R., 2 H. L. 99 (1867); Ross v. Estates, &c., Co., L. R., 3 Chan. App. 682 (1868);

Askew's Case, L. R., 9 Id. 664 (1874); Cargill v. Bower, L. R., 10 Chan. Div. 502, (1878); Henderson v. Lacon, L. R., 5 Eq. 249; Smith v. Reese, L. R., 2 Id. 264 (1866); Thorpe v. Hughes, 3 Mylne & Cr. 742 (1838); Waldo v. Chicago, &c., R. R. Co., 14 Wis. 575 (1861); Henderson v. Railroad Co., 17 Texas, 560 (1856); State v. Jefferson, &c., Co., 3 Humph. 305 (1842); Ashmead v. Colby, 26 Conn. 287 (1857).

³ State v. North Louisiana, &c., R. R. Co., 34 La. Ann. 947; People's Bank v. Kurtz, 99 Penn. St. 344 (1882); Seizer v. Mali, 41 N. Y. 619 (1869).

⁴ Kempson v. Saunders, 4 Bing. 5 (1826); Nockles v. Crosby, 3 Barn. & C. 814 (1825); Gompertz v. Bartlett, 2 El. & Bl. 849 (1853); Kendall v. Stone, 5 N. Y. 14 (1851).

⁵ Kent v. Quicksilver Mining Co., 78 N. Y. 139; Thomas v. Railroad Co., 101 U. S. 71. And where a corporate officer issues illegal and unauthorized stock, he may be enjoined from allowing a transfer of it, if proof is given of its illegal character and of a proposed transfer. Sherman v. Clark, 4 Nev. 138 (1869).

with the overissue of the stock are fully and finally determined and adjudicated, and the overissued stock itself is retired and destroyed. Such a proceeding is in the nature of a bill to quiet title, or to remove a cloud from the title of the genuine stock. Spurious or overissued stock, issued by corporate officers having the apparent authority, and outstanding in the hands of numerous holders, is a cloud upon the title to the genuine stock. It is a cloud which a court of equity will remove, and a suit to that end may be commenced, either by the corporation on behalf of the shareowners,¹ or by the stockholders themselves in their own behalf, the corporation failing or refusing to institute it.²

§ 298. *Subscriber's right to defeat a subscription to over-issued stock, and to recover back money paid thereon.*—In addition to the remedy in equity, the holder of overissued stock has the further right at law to defeat an action on his subscription therefor, and that, too, even though he knew it to be over-issued at the time the subscription was made. There can be no estoppel in such a case, and not even creditors can enforce any liability on spurious or overissued stocks.³ Where also a subscriber has paid an installment on his subscription, although he knew when he made the subscription and paid the money, that it was an illegal and unauthorized issue, he may rescind and recover back what he has paid.⁴ In Iowa, it has been held, that payment of a note given for overissued stock cannot be enforced where the consideration was expressed in the note to be the stock of the corporation to which the note was given, and the direc-

¹ New York, &c., *R. R. Co. v. Schuyler*, 17 N. Y. 592 (1858); *Plimpton v. Bigelow*, 93 Id. 592, 602 (1883).

² *Dewing v. Perdicaries*, 96 U. S. 193 (1877); *Wood v. Union, &c., Assn.*, 63 Wis. 9 (1885); *Perdicaris v. Charleston Gaslight Co.*, Chase's Dec. 435 (1869). *Cf. Taylor v. South & North Ala. R. R. Co.*, 4 Woods, 575 (1882), where the subscriber acquiesced ten years. The court denied any relief.

³ *Scovill v. Thayer*, 105 U. S. 143 (1881); *Page v. Austin*, 10 Can. Sup. Ct. 132; *Clark v. Turner*, 73 Ga. 1 (1884).

⁴ *Knowlton v. Congress, &c., Co.*, 14 Blatch. 364 (1877); *aff'd* 103 U. S. 49 (1880); *Thomas v. City of Richmond*, 12 Wall. 349, 355 (1870); *Walker v. Chap-*

man, Lofft, 342; *Lowry v. Bourdieu*, Doug. 468; *Tappenden v. Randall*, 2 Bos. & P. 467 (1801); *Hastelow v. Jackson*, 8 Barn. & C. 221 (1828); *Aubert v. Walsh*, 4 Taunt. 293 (1812); *Busk v. Walsh*, 4 Id. 290 (1812); *Bone v. Ekless*, 5 Hurl. & N. 925 (1860); *White v. Franklin Bank*, 22 Pick. 181 (1839); *Reed v. Boston Machine Co.*, 141 Mass. 454 (1886); *Nellis v. Clarke*, 4 Hill, 424 (1842); *Morgan v. Groff*, 4 Barb. 524 (1848); *Taylor v. Bowers*, 1 Q. B. Div. 291; s. c. 34 L. T. (N. S.) 938. And the dissenting opinion of Dwight, Comr., in *Knowlton v. Congress, &c., Co.*, 57 N. Y. 518, 540 (1874). This case, however, was not strictly a case of overissued stock.

tors subsequently made an illegal and unauthorized increase in the stock, the maker of the note having had notice that a large amount of illegal stock had been issued, and that the illegal and valid stock could not be distinguished.¹ But it is held that one who subscribes for overissued stock, *bona fide*, upon discovering that the stock is spurious, cannot have a receiver appointed, pending an inquiry into the legality of the stock, to the end that, in case the stock be judicially declared invalid, such subscriber may recover back from the corporation the money so paid for the spurious shares, when the money received by the company had not been kept separate from its general funds, and could not be traced and identified.²

¹ Merrill v. Gamble, 46 Iowa, 615 (1877); Merrill v. Beaver, 46 Id. 646 (1877); Merrill v. Reaver, 50 Id. 404 (1879). ² Whelpley v. Erie Railway Co., 66 Blatch. 271 (1868).

PART II.

TRANSFERS OF STOCK.

CHAPTER XVIII.

LEGACIES AND GIFTS OF STOCK.

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| <p>§ 299. Definitions of general, specific, and demonstrative legacies of stock.</p> <p>300-301. Importance of the difference between general and specific legacies.</p> <p>302-303. Legacies of stock are construed to be general, if the language will permit.</p> | <p>§ 304-305. Amount of stock conveyed by certain legacies.</p> <p>306. Ademption or revocation of a legacy of stock, and abatement.</p> <p>307. Duty of executor as regards specific or general legacies.</p> <p>308. Gifts of stock.</p> |
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§ 299. *Definitions of general, specific, and demonstrative legacies of stock.*—A general legacy of stock is a legacy whereby it becomes the duty of the executor or administrator to give to or procure for the legatee a certain amount of stock, as indicated by the will, there being nothing in the will itself to indicate that the legacy is to be satisfied by stock actually owned by the testator. A specific legacy of stock arises when the testator, in his will, directs or clearly indicates that the legacy is to be satisfied from stock which he owns.¹ A demonstrative legacy of stock is the same as a general legacy, except that it is to be purchased from a particular fund of the estate. Demonstrative legacies of stock are of little importance as compared with the other two kinds.²

§ 300. *Importance of the difference between general and specific legacies.*—It is frequently of the greatest importance whether

¹ On this subject in general, see Roper on Legacies (2d ed.); Jarman on Wills; Williams on Executors; Bouvier Law Dic., vol. II, p. 60; Tift v. Porter, 8 N. Y. 516 (1853), where the court says: "A legacy is general where it is so given as not to amount to a bequest of a particular thing or money of the testator, distinguished from all others of the same kind. It is specific when it is a bequest of a specific part of the testator's personal estate, which is so distinguished."

² That legacies of stock may be demonstrative has been assumed by the cases. In the case, however, of Eckfeld's Estate, 7 W. N. C. (Penn.) 19 (1879), the court says a legacy of stock "may be either specific or general, according to the circumstances. It is never demonstrative. A demonstrative legacy is always pecuniary, differing, however, from an ordinary legacy in being referred to a particular fund or source of payment."

a legacy be a general or a specific one. A long line of decisions, running back for nearly two hundred years, have been made in endeavoring to lay down rules on this subject. The complications, contradictions, inconsistent decisions and doubt that have arisen from the inherent difficulties of the subject are frequently adverted to and deplored by successive generations of judges.

The importance of determining whether a legacy of stock is general or specific rests in the fact that if it is specific it is entitled to certain advantages, and, on the other hand, is exposed to certain perils; while, if it is general, it is without those advantages, but is also free from the perils. The advantages of a legacy of stock being specific are that debts of the estate are to be paid from other funds; the specific legacy passes, though other legacies fail partially or wholly by reason of deficiencies in the estate; and the specific legatee is entitled to all dividends declared after the testator's death, instead of losing the first year's dividends, as in case of a general legacy of stock. General legacies of stock have none of these advantages. On the other hand, a specific legacy of stock is open to the great danger of being revoked by the acts of the testator, and frequently so when the testator has no intention of revoking the legacy.¹ This revocation, arising by implication from the acts of the testator, such as selling the stock bequeathed, or using it in any way inconsistent with the idea of its passing under the will, is a danger that does not exist if the legacy is a general one, since general legacies of stock may be carried out by the executor's purchasing the stock for the purpose of the legacy.

¹ *Kenkel v. Macgill*, 56 Md. 120 (1880), the court saying: "If the legacy is to be considered specific, then, in the event of the testator's parting with the thing or property bequeathed, or if from any cause it should be lost or destroyed, the legacy fails. Then, again, such legacies are not liable to abatement with general legacies, nor are they liable to contribution towards the payment of debts." Where evidently the intent was to give specific bonds, it was so decreed.

Davies v. Fowler, L. R. 16 Eq. 308 (1873); *Walton v. Walton*, 7 Johns. Ch. 257 (1823); *Jacques v. Chambers*, 2 Coll. 435 (1846), holding also that the legatee may select his stock from different classes, but that he must pay calls on the stock due at the time of the testator's death but

not paid. In the case *Mullins v. Smith*, 1 Dr. & Sm. 204 (1860), the difference between a specific and demonstrative legacy is thus described:

"The points of difference between specific and demonstrative legacies are these:

"A specific legacy is not liable to abatement for the payment of debts, but a demonstrative legacy is liable to abate when it becomes a general legacy by reason of the failure of the fund out of which it is payable. A specific legacy is liable to ademption, but a demonstrative legacy is not. A specific legacy, if of stock, carries with it the dividends which accrue from the death of the testator, while a demonstrative legacy does not carry interest from the testator's death."

§ 301. If a specific legacy will apply equally to paid-up stock and to stock not paid up, the legatee may take the former.¹ If the testator has made payments on the stock before calls have been made, the legatee is entitled to the benefit.² If there is both a specific and a general legacy of the same stock, the specific is to be first satisfied.³ The specific legatee takes all the income and profits of the stock,⁴ whereas the general legatee has no interest in the stock until twelve months after the testator's death.⁵ The specific legatee takes the stock, although there will then be no property left to pay pecuniary legacies.⁶ However, he can have only so much stock of that kind as the testator dies possessed of,⁷ and if the latter dies possessed of none, the specific legatee takes none.⁸ The specific legatee does not take dividends declared and due before the testator's death, although such dividends have not been collected.⁹

§ 302. *Legacies of stock are construed to be general, if the language will permit.*—It is the policy of courts of justice to uphold and carry out a legacy, and implied revocations are not looked upon with favor. Accordingly, in order to avoid the danger of ademption, to which specific legacies are subject, the rule has become established that general legacies are to be favored by the courts, and if there is doubt as to whether a legacy be specific or general, it will be construed to be of the latter kind.¹⁰

¹ Millard v. Bailey, L. R. 1 Eq. 378 (1866); Jacques v. Chambers, *supra*.

² Tanner v. Tanner, 11 Beav. 69 (1848).

³ Barton v. Cooke, 5 Ves. 461.

⁴ Loring v. Woodward, 41 N. H. 391 (1860), holding also that parol evidence cannot show a contrary intent of the testator.

⁵ Webster v. Hale, 8 Ves. 410 (1803).

⁶ Drinkwater v. Falconer, 2 Ves. Sr. 622 (1755).

⁷ Gordon v. Duff, 28 Beav. 519 (1860); Ashton v. Ashton, 3 P. Wms. 384 (1735).

⁸ Evans v. Trip, 6 Mad. 91 (1821).

⁹ Perry v. Maxwell, 2 Dev. Eq. (N.C.) 487 (1834).

¹⁰ Davies v. Fowler, L. R. 16 Eq. 308 (1873), where the court says:

"With regard to specific legacies, the doctrines of this court are very minute, and very refined distinctions are drawn, and no doubt the general inclination is to treat a legacy as general rather than as specific. This construction is

generally in favor of the legatees, because, although a specific legatee has many advantages, he is exposed to many perils.

"He has the advantage of taking the very thing that is given, although the general assets may be insufficient; and he has the advantage of taking the dividends or interest from the death of the testator. But, on the other hand, he is exposed to the very great peril of ademption."

Tift v. Porter, 8 N. Y. 516-520, where the court says: "The inclination of the courts to hold legacies to be general rather than specific, and on which the rule is based, that to make a legacy specific its terms must clearly require such a construction, rests upon solid grounds. The presumption is stronger, that a testator intends some benefit to a legatee, than that he intends a benefit only upon the collateral condition that he shall remain, till death, owner of the property bequeathed." To same effect see *Eckfeld's Estate*, 7 W. N. C. (Penn.) 19 (1879).

Where, however, the intent of the testator clearly was to give particular stock owned by him, the court will declare the legacy to be a specific one. Thus, where the testator gives the legacy of stock by describing it as "my" stock, the legacy is a specific one.¹ So also where the phrase is used, "standing in my name;"² or, "which I hold;"³ or a direction is given to make up the specified amount from the general fund if the testator does not hold enough;⁴ or the testator describes the stock as "now lying in the 3 per cents.;"⁵ or uses the word "such;"⁶ or makes a legacy of stock out of a quantity of stock;⁷ or in another part of the will speaks of the stock as that of which the testatrix may die possessed;⁸ or where, after several legacies, all apparently general, the testator bequeathes the remaining stock "standing in my name;" the effect of all these is that the legacies are specific.⁹ A legacy of all the dividends, interest, and proceeds from stock is a specific legacy, even though the testator did not own such stock

¹ *Walton v. Walton*, 7 Johns. Ch. 257 (1823); *Loring v. Woodward*, 41 N. H. 391 (1860); *Shuttleworth v. Greaves*, 4 Mylne & Cr. 35 (1838); *Miller v. Little*, 2 Beav. 259 (1840); *Hayes v. Hayes*, 1 Keen, 97 (1836); *Brainerd v. Cowdrey*, 16 Conn. 1 (1843). The omission of the word "my" does not necessarily make the legacy a general one. *Avelyn v. Ward*, 1 Ves. Sr. 420 (1749). The word "my" does not, however, have the same significance in its application to a legacy of an annuity as it has to a legacy of stock. *Kirby v. Potter*, 4 Ves. 748 (1799). In the case *Parrott v. Worsfold*, 1 Jac. & Walker, 574 (1820), a legacy of "all my stock that I may be possessed of at my decease," was held to be general since there was no "individual thing given."

² *Ludlam's Estate*, 13 Penn. St. 188 (1850); *Gordon v. Duff*, 28 Beav. 519 (1860); *Kampf v. Jones*, 2 Keen. 756 (1837). Where, however, other parts of the will indicate that the legacy was general, it was held to be general. See *Auther v. Auther*, 13 Sim. 422 (1843), holding also that, though by the delay of the executor beyond a year in purchasing the stock, it rises, the legatee is entitled to the same amount as if it had been bought at the right time. *Fidelity Trust Company's Appeal* (Penn., Oct., 1885).

³ *Blackstone v. Blackstone*, 3 Watts, 335 (1839).

⁴ *Townsend v. Martin*, 7 Hare, 471 (1849), holding that such a legacy is

specific and not demonstrative. The case, however, of *McGuire v. Evans*, 5 Ired. Eq. (N. C.) 269 (1848), holds that a legacy of stock, to take effect in case other legacies do not absorb that stock, is demonstrative; also that in case of legacies of the same stock to two different persons, each takes a moiety. The case of *Mulling v. Smith*, 1 Dr. & Sm. 204 (1860); *Fontaine v. Tyler*, 9 Price Ex. 94 (1821); and *Queen's College v. Sutton*, 12 Sim. 521 (1842), hold that such a legacy is specific if the testator leaves stock enough, but is general if he does not leave enough.

⁵ *Morely v. Bird*, 3 Ves. 628 (1800), and holding that if the executor has sold the stock the legatee may hold him liable for its value one year after the testator's death.

⁶ *Davies v. Fowler*, L. R. 16 Eq. 308 (1873), the court saying that a legacy is specific when a meting out or dividing is evidently intended.

⁷ *Hasking v. Nicholls*, 1 Y. & C. Ch. 478 (1842), and if the administrator has paid the dividends to another, he is personally liable.

⁸ *Measure v. Carleton*, 30 Beav. 538 (1862). This case also holds that if an exact partition of the stock is impossible, enough will be sold so as to render it possible.

⁹ *Sleece v. Thorington*, 2 Ves. Sr. 560 (1754).

at the time he made the will.¹ There has been some difference of opinion as to whether the fact that the testator, at the time of making the will, possessed an equal or greater amount of stock than that bequeathed, and of the same kind, is to be taken as evidencing an intent to make the legacy specific. The weight of authority holds that such a fact is not to be taken into consideration, and that if the words of the legacy make it general, it cannot be construed to be specific simply because by an examination of the testator's effects, he is found to have possessed stock similar to that described in the will.²

§ 303. The most common form of a general bequest of stock is where the testator merely bequeathes a specified number of shares of a specified kind to the legatees, without any further words indicating that he then held or expected to hold the stock bequeathed.³ A direction to the executors to invest a certain sum in specified stock for the benefit of the legatee is a general legacy.⁴ So also where the executors are directed to transfer to the legatee certain stock.⁵ A legacy of the residue of the testa-

¹ *Stephenson v. Dawson*, 3 Beav. 342 (1840). See also *Fidelity Trust Company's Appeal* (Penn., Oct., 1885).

² *Robinson v. Addison*, 2 Beav. 515 (1840), the court holding that the legacy was general, and saying the testator "in effect gave such an indefinite sum of money as would suffice to purchase so many shares as he had given." *Davis v. Cain's Exr.*, 1 Ired. Eq. (N. C.) 304 (1840); *Bransdan v. Winter*, Ambl. 56 (1738); *Simmons v. Vallance*, 4 Brown's Ch. 346 (1793); *Bishop of Petersborough v. Mortlock*, 1 Brown's Ch. 565 (1784); *Boys v. Williams*, 2 Russ. & Myl. 689 (1831); *Partridge v. Partridge*, Cases Temp. Talbot, 226 (1736); *Tiff v. Porter*, 8 N. Y. 516 (1853), where the court says: "The mere possession by the testator, at the date of his will, of stock of equal or larger amount than the legacy, will not, of itself, make the bequest specific." *Osborne v. McAlpine*, 4 Redf. (N. Y. Surr.) 1 (1878); *Eckfeld's Estate*, 7 W. N. C. (Penn.) 19 (1879); *Sponsler's Appeal*, 107 Penn. St. 95 (1884), where the court also held that a codicil repeating a general legacy of stock will entitle the legatee to both legacies. In Massachusetts a doctrine contrary to that stated in the text, prevails. See *White v. Winchester*, 23 Mass. 48 (1827); *Metcalf v. First*

Parish, 128 Mass. 370 (1880). To same effect, *Cuthbert v. Cuthbert*, 3 Yeates (Penn.), 486 (1803); *Jeffreys v. Jeffreys*, 3 Atk. 120 (1744).

³ *Wilson v. Brownsmith*, 9 Ves. 180 (1803), holding also that if there is not enough of such stock among the testator's assets, the deficiency must be purchased for the legatee. *Pearce v. Billings*, 10 R. I. 102 (1871), the court saying that the evident intent of the testator was "to have the stock mentioned purchased for the legatees by his executor, or to have the legatees furnished with the means to purchase the stocks for themselves." The value of the stocks one year after the testator's death is the amount to be paid to the legatees. In the case of *Purse v. Snaplin*, 1 Atk. 413 (1737), where two legacies of 5,000*l* each were given, and the testator had but 5,000*l* of stock, the court held that the general estate must purchase 5,000*l* of the same stock.

⁴ *Raymond v. Brodbelt*, 5 Ves. 199 (1880).

⁵ *Lambert v. Lambert*, 11 Ves. 607 (1805); *Sibley v. Perry*, 7 Ves. 522 (1802), the court saying, a legacy is not specific "without something marking the specific thing, the very corpus; without describing it, as standing in his name, or by the expression, 'my stock,' &c."

tor's stock has been held to be a general legacy.¹ A legacy to be paid "out of the four per cents." is general.² A codicil which is general in form, is held to be such, although it is but an increase of a previous legacy which is specific, and which is revoked by the codicil.³

§ 304. *Amount of stock conveyed by certain legacies.*—A legacy of "one hundred pounds, long annuities" has been held to mean, not that the legatee is entitled to an annual income from the estate of one hundred pounds, but that he was entitled to have that amount invested for him.⁴ A will reciting the amount of stock held by the testatrix, and bequeathing it, or so much as should be standing in her name at her death, does not give to the legatee stock acquired after the making of the will, and before the death of the testatrix.⁵ A bequest of stock "that I possess" is held to mean stock possessed by the testator at the time of making the will.⁶

§ 305. There has been some controversy and doubt as to whether a legacy of the testator's "money" would give to the legatee the testator's stock in a corporation. The decided weight of authority holds that it does not.⁷ Nor will shares of stock be-

¹ Parrott v. Worsfold, 1 Jac. & W. 574 (1820). *Contra*, Bethune v. Kennedy, 1 Myl. & C. 114 (1835).

² Deane v. Test, 9 Ves. 146 (1803).

³ Johnson v. Johnson, 14 Sim. 313 (1844).

⁴ Atty. Gen. v. Grote, 2 Russ. & Myl. 699 (1831); Fonnereau v. Payntz, 1 Bro. Ch. 412 (1785). See Pearce v. Billings, *supra*. *Contra*, Stafford v. Horton, 1 Bro. Ch. 421 (1785).

⁵ Hotham v. Sutton, 15 Ves. 319 (1808). So also of a legacy of "the whole of my stock in the Housatonic Bank, amounting to \$6,000." The legatee does not take stock subsequently acquired. Foote, Appellant, 39 Mass. 299 (1839); Douglass v. Douglass, Kay, 404. The case of Fidelity Trust Company's Appeal (Super. Ct. Penn. October, 1885), states that at common law a specific legacy of stock spoke from the death of the testator, and that the English Wills Act of 1838, and the Pennsylvania act of 1879, were but declaratory in that respect. If the testator, in making a specified bequest of stock, speaks of the stock as

"now standing in my name," the statute does not apply, and the bequest speaks from the date of the will. In Miller v. Miller, 2 Beav. 259 (1840), the testator gave "one share to each child, him surviving." He then had eight shares and seven children. At his death he had ten shares and eleven children. Only the eight shares were held to pass.

⁶ Cochran v. Cochran, 14 Sim. 248 (1844). This rule is sometimes changed by statute. See in England, § 24, Wills Act, applied in Trinder v. Trinder, L. R., 1 Eq. 695 (1866), and Goodlad v. Burnett, 1 K. & J. 341; Hepburn v. Skerving, 4 Jur. N. S. 651; Wagstaff v. Wagstaff, L. R., 8 Eq. 229; Bothamley v. Shersan, L. R., 20 Eq. 304.

⁷ Mullins v. Smith, 1 Dr. & Sm. 204 (1860); Hotham v. Sutton, 15 Ves. 319 (1808); Lowe v. Thomas, Kay, 369; *aff'd*, 5 De G., M. & G. 315 (1854); Gosden v. Dotterill, 1 Myl. & K. 56 (1832); Hundleston v. Gouldsbury, 10 Beav. 547 (1847); Douglas v. Congreve, 1 Keen, 410, 424 (1836); Willis v. Plaskett, 4 Beav. 208 (1841); Ogle v. Knipe, L. R., 8 Eq. 436

long to a legatee to whom the testator has given, by a last will and testament, his "securities for money,"¹ or "furniture," and all claims and demands of whatever nature,² or "every other article,"³ or "ready money,"⁴ or goods,⁵ or "money and effects,"⁶ but they will pass under a bequest of the "personal estate,"⁷ or "residue of money,"⁸ or "chattels."⁹ If the testator, in describing the stock bequeathed, has very clearly made a mistake in the description, the legacy will be held to apply to the stock intended to be bequeathed. Thus where the testator has "city bank" stock, but bequeaths "mechanics bank" stock, and the intent clearly was to bequeath the former, the court will render a decree to that effect.¹⁰ Where, subsequently to the making of the will, and before the death of the testator, the stock bequeathed is changed in its character by operation of law, the legatee will nevertheless be entitled to the stock in its new form.¹¹ In England, where "shares" corresponds to the American "stock," but "stock" is a term applicable to a paid-up interest which, like a bank deposit, may be used in large or small quantities, a bequest of "shares" does not pass "stock" if there be any "shares" to which the legacy may apply.¹² The words "funds" or "public

(1869); *Ommaney v. Butcher*, 1 Tur. & R. 260, 272 (1823), holding also that a bequest of stock for an indefinite charity fails. *Beck, Ex. v. McGillis*, 9 Barb. 35, 39 (1850). *Contra*, *Waite v. Coombes*, 5 De G. & S. 676 (1852); *Chapman v. Reynolds*, 28 Beav. 221 (1860), where the testator had no property but stock. *Bescoby v. Pack*, 1 Sim. & Stu. 500 (1823), holding that "money" will pass the "funds," but not stock in private corporations. *Newman v. Newman*, 26 Beav. 218 (1858), where the legacy was of "surplus money." *Jenkins v. Fowler*, (N. H. March, 1886).

¹ *Turner v. Turner*, 21 L. J. (Ch.) 843 (1852).

² *Delamater's Estate*, 1 Whart. (Penn.) 362 (1836).

³ *Collier v. Squire*, 3 Russ. 467 (1827).

⁴ *May v. Grave*, 3 De G. & Sm. 462 (1849).

⁵ *Cowling v. Cowling*, 26 Beav. 449 (1859). *Contra*, *Kendall v. Kendall*, 4 Russ. Ch. 360 (1823).

⁶ *Borton v. Dunbar*, 30 L. J. (Ch.) 8 (1861).

⁷ *Kermode v. Macdonald*, L. R., 3 Ch. 584 (1868).

⁸ *Dawson v. Gaskoin*, 2 Keen, 14 (1837); *Fulkeron v. Chitty*, 4 Jones' Eq. (N. C.) 244 (1858).

⁹ *Kendall v. Kendall*, *supra*.

¹⁰ *Roman Catholic Orphan Asylum v. Emmons*, 4 Redf. (N. Y.) 144 (1855); *Door v. Geary*, 1 Ves. Sr. 255 (1749), holding that a bequest of "East India stock" will apply to bank stock, when the testator had the latter but none of the former. See also *Trinder v. Trinder*, L. R., 1 Eq. 695 (1866), where a legacy of "Great Western Railway" stock was held to apply to the stock of a road absorbed by the Great Western Railway. *Oakes v. Oakes*, 9 Hare, 666 (1852), where a bequest of "shares" was held to apply to "stock." *Gallini v. Noble*, 3 Mer. Ch. 690; *Penticost v. Ley, J. & W.* 207; *Clark v. Atkins*, 90 N. C. 629, where "bank stock" was held to pass bonds.

¹¹ See § 306, note 9.

¹² *Oakes v. Oakes*, 9 Hare, 666 (1852).

funds," will include long annuities;¹ and "foreign funds" means securities guaranteed by foreign governments,² but "funds" will not include bank stock,³ nor East India stock.⁴ An unconditional bequest of the dividends of stock is a bequest of the stock itself.⁵ But a bequest of a specific sum to be paid from stock does not bequeath the stock itself, although amounting to a charge upon it.⁶ A bequest of stock to a legatee "to draw the income arising therefrom, during her lifetime, and at her death to dispose of the same as she shall see fit," vests the title to the stock, when it is set apart, in the legatee, even though the executors are directed to collect and pay to her the dividends.⁷ A bequest of the "rest and residue after deducting" certain specific legacies of stock, includes those legacies, if they have lapsed by reason of the death of the legatees.⁸ A general bequest of stock applies to full paid as well as partly paid stock.⁹ Legacies may be made of stock over which the testator has the power of appointment,¹⁰ and a will may provide for an annuity to be derived from stock.¹¹

§ 306. *Ademption or revocation of a legacy of stock, and abatement.*—The ademption of a legacy is a revocation of that

¹ Howard v. Kay, 27 L. J. (Ch.) 448 (1858).

² Ellis v. Eden, 23 Beav. 543 (1857); Cadett v. Earle, L. R. 5 Ch. D. 710 (1877), properly holding that New York and Ohio are foreign governments. Cf. Longdale's Settlement Trusts, L. R., 5 Ch. D. 710 (1877), relative to French railway securities.

³ Slingsby v. Granger, 7 H. L. Cases, 273 (1859).

⁴ Brown v. Brown, 4 K. & J. 704 (1858).

⁵ Collier v. Collier, 3 O. St. 369; Haig v. Swiney, 1 Sim. & Stu. 487 (1823); Page v. Leapingwell, 18 Ves. 463 (1812); Fox v. Carr, 16 Hun, 566 (1879), involving a similar question. Cf. Blann v. Bell, 2 De G., M. & G. 775 (1852), holding that this rule applies only to the "funds," but not to stock in private corporations.

⁶ Wilson v. Maddison, 2 Y. & C. Ch. 372 (1843).

⁷ Onondaga Trust & Deposit Co. v. Price, 87 N. Y. 542 (1882).

⁸ Carter v. Taggart, 16 Sim. 423 (1848); Shuttleworth v. Greaves, 4 Myl. & Cr. 35 (1838), holding that a legacy of stock lapses as to those dying before the testator, though it is given to them,

"their executors, administrators, or assigns."

⁹ Emery v. Wason, 107 Mass. 507 (1871). This case holds also that where a call on the stock becomes due the day after the testator died, it was the duty of the executor to pay it from the general fund.

¹⁰ See *Re David's Trusts*, 1 Johns. 495 (1859); *Innis v. Sayer*, 3 Mac. & G. 606 (1851); *Lawnds v. Lawnds*, 1 You. & Jer. 445 (1827); *Nannock v. Horton*, 7 Ves. 391 (1802). *Re Gratwick's Trusts*, L. R. 1 Eq. 177 (1865); *Warren v. Pastlewaite*, 2 Coll. Ch. 116 (1845); *Walker v. Mackie*, 4 Russ. 16 (1827), disapproved in *Hughes v. Turner*, 3 Myl. & K. 697 (1834).

¹¹ As to the construction of different provisions in wills, where an annuity on stock is created, see *Innes v. Mitchell*, 9 Ves. 212 (1803); *Kerr v. Middlesex Hospital*, 2 De G., M. & G. 576 (1852); *Ross v. Borer*, 2 Jo. & H. 469 (1862); *Yates v. Maddan*, 3 Mac. & G. 532 (1857); *Blewitt v. Roberts*, Cr. & Ph. 274 (1841); *Potter v. Baker*, 13 B. 273 (1851); *Robinson v. Hunt*, 4 B. 450 (1841); *Hedges v. Harpur*, 3 De G. & J. 129 (1858); *Evans v. Jones*, 2 Collyer, 516 (1846); *Manserge v. Campbell*, 3 De G. & J. 232.

legacy in part or wholly, not by an express revocation in the will, but by the acts of the testator. Consequently an ademption applies only to specific legacies. An ademption of a specific legacy of stock generally arises by a sale of the stock by the testator. If the specific stock bequeathed is not owned by the testator at the time of his death, the legal conclusion is that the specific legacy is adeemed, and the legatee takes nothing.¹ A sale of the stock by the testator after the will is made revokes or adeems the legacy, and it is as if never made.² A codicil giving all the "personal estate" to another is a revocation of a bequest of stock in the original will.³ Where the testator specifies the amount of his stock, the specific legatees of it abate proportionately with the residuary legatee, where upon his death it is insufficient.⁴ The rule is otherwise if no mention is made of what amount of stock he owns.⁵ If the general property of the testator is exhausted in the payment of the debts of the estate, specific legacies of stock abate proportionately with other specific legacies.⁶ A specific legacy of stock is not adeemed by a change in the stock, produced by an act of the government. Thus, where the government buys the stock, a specific legatee takes the compensation if it has not yet been collected by the testator,⁷ but not if it has been collected and used by the latter.⁸ A change by law of the funds into funds bearing a lower rate of interest does not adeem a specific legacy of it,⁹ even though the testator sells the former and buys the latter kind of funds.¹⁰ A specific legacy of stock by a *feme covert*,

¹ *Ford v. Ford*, 23 N. H. 212 (1851), although not a stock case, says in regard to this branch of the law: "It is now established in England that the only question is whether the specific thing remains at the death of the testator, and that the intention to adeem will not be considered beyond the expressions in the will. . . . The weight of American authority is in favor of the English rule."

² *Ashburner v. Macguire*, 2 Brown's Ch. 108 (1786); *White v. Winchester*, 23 Mass. 48 (1827); *Humphreys v. Humphreys*, 2 Cox, 184 (1789); *Hayes v. Hayes*, 1 Keen, 97 (1836); *Blackstone v. Blackstone*, 3 Watts, 335 (1839).

³ *Kermode v. Macdonald*, L. R. 1 Eq. 457 (1866); *aff'd*, L. R. 3 Ch. 584 (1868).

⁴ *Elwes v. Causton*, 30 Beav. 554 (1862); following *Page v. Leapingwell*, 18 Ves. 463 (1812).

⁵ *Petre v. Petre*, 14 Beav. 197 (1851);

De Lisle v. Hodges, L. R. 17 Eq. 440 (1874); *Vivian v. Mortlock*, 21 Beav. 252 (1855). The debts of the estate may be directed to be paid from the residue of the stock. *Choat v. Yeates*, 1 Jac. & Walk. 102 (1819).

⁶ *Sparks v. Weedon*, 21 Md. 156 (1863). When general legacies of stock abate proportionately with other general legacies, the stock is estimated at its value twelve months after the testator's death. *Blackshaw v. Rogers*, cited in 4 Brown's Ch. 349.

⁷ *Walton v. Walton*, 7 Johns. Ch. 257 (1823).

⁸ *Ludlam's Estate*, 13 Penn. St. 188 (1850).

⁹ *Brown v. McGuire*, 1 Beat. Ir. Ch. 358 (1829).

¹⁰ *Partridge v. Partridge*, cases temp. Talbot, 226 (1736). *Roper on Legacies*, p. 331, 2d ed. (1848), is inclined to the

who had the power to bequeath it, is not adeemed by the fact that she had the stock transferred into her own name after the death of her husband.¹

§ 307. *Duty of executor or administrator as regards a specific or general legacy of stock.*—Where a legacy of stock is given it is the duty of the executor or administrator to carry into effect the wishes of the testator by turning over to the legatee the stock bequeathed if the legacy be specific, or if the legacy be general by either setting aside for the legatee the required amount of stock from the testator's effects, or purchasing the same for the legatee. The specific legacy of stock vests in the legatee as soon as the executor is satisfied that the general fund will pay the debts of the estate and consents to such vesting. When once given the consent of the executor is irrevocable and only a Court of Chancery can reach the stock and subject it to the testator's debts.²

§ 308. *Gifts of stock.*—Shares of stock in a corporation may be the subject of a gift. No formal method of carrying out the gift is necessary. A formal instrument of transfer, duly delivered to an agent with directions to deliver to the donee, vests title in the donee, though no certificates are transferred.³ A gift of stock, vested by a due transfer into the name of the donee, cannot be revoked by the donor.⁴ In order to constitute a gift a perfectly clear intent so to do must be proved.⁵ Where the gift is made in gratitude for care to be bestowed on another, the gift will fail upon the death of the donee, it being proved that the stock had not been fully and finally delivered.⁶ A gift of the

opinion that a specific legacy of stock is not revived by a purchase of similar stock after a sale of the stock bequeathed.

¹ *Dingwell v. Askew*, 1 Cox's Ch. 427 (1788).

² *Onondaga Trust & Deposit Co. v. Price*, 87 N. Y. 542 (1882); *Hill v. Rockingham Bank*, 44 N. H. 567 (1863), holding that the legatee should sue the corporation at law for refusing transfer where the parties interested in the will assent; and in equity if both the corporation and such parties do not assent. A decree of a probate court that the legacy of stock shall be turned over to the legatee cannot be required by the corporation. Under the Vermont statute it is the duty of the executor to transfer stock to the resid-

uary legatee. *Witters v. Sawles*, 25 Fed. Rep. 168 (1885).

³ *De Caumont v. Bogert*, 36 Hun, 382 (1885), treating also of a gift as an advancement.

⁴ *Standing v. Bowring*, L. R. 27 Ch. D. 341 (1884), where the donor transferred into the joint names of donor and donee, and afterwards attempted to dispose of the whole stock.

⁵ Where, however, the stock is purchased by one in the name of another, parol evidence may show as against the creditors of the former that he intended the stock as a gift to the latter. *Rider v. Kidder*, 10 Ves. 361 (1805).

⁶ *Jackson v. Twenty-third St. Ry. Co.*, 88 N. Y. 520 (1882). When a gift of

dividends of stock is a gift of the stock itself.¹ A gift of stock by one legatee to another, in the belief that the testator so intended the stock to be disposed of, cannot be revoked after an unsealed instrument of transfer is signed and actual transfer made, even though it is afterwards found that the testator had no such intent.² A stockholder who has transferred his stock into the joint names of himself and his wife cannot dispose of his interest by a last will and testament. It passes to the wife as the survivor.³ A gift of stock, *donatio causa mortis*, may be made by a mere delivery of the certificate to the donee.⁴ So, also, the delivery and acceptance of a gift of stock is held to be effectual where the donor had the stock transferred into the name of the donee and took out certificates in the donee's name, even though the donor died before the donee knew of the gift.⁵

stock is made in accordance with an agreement to compensate the donee for taking care of the donor, a delivery of the certificate without any transfer suffices. *Reed v. Copeland*, 50 Conn. 472 (1883). But the contract to make the gift must not be in opposition to public policy, nor in fraud of the rights of other stockholders. *Nickerson v. English*, 6 East. Rep. 651 (Mass. 1886).

¹ See § 305.

² *Delamater's Estate*, 1 Whart. (Penn.) 362 (1836).

³ *Dummer v. Pitcher*, 5 Sim. 35 (1831); *aff'd* 2 M. & K. 262 (1833). A gift of stock direct from the husband to the wife is legal. She thereupon takes a sole and separate estate therein. *Deming v. Williams*, 26 Conn. 226 (1857). The case of *Francis v. New York & B. El. R. R. Co.*, 17 Abb. N. C. 1 (N. Y. 1885), holds that when a gift of stock is made to a minor, it is complete and irrevocable, so far as the donor is concerned, but the minor may, upon attaining majority, either accept or refuse it.

⁴ *Grymes v. Hone*, Exr. 49 N. Y. 17 (1872); *Walsh v. Sexton*, 55 Barb. 251 (1869); *Allerton v. Lang*, 10 Bosw. 362

(1863). The last two cases hold that the certificates need not even be endorsed or transferred, but that a mere delivery without any writing is sufficient. A *donatio causa mortis* of stock is revoked by the recovery of the donor, even though it is registered. *Stainland v. Willott*, 3 Mac. & G. 664 (1850). In England railway stock is not the subject of a *donatio causa mortis*, by a delivery of the certificate, since the transfer can be by deed only. *Moore v. Moore*, 43 L. J. (Ch.) 617 (1874).

⁵ *Robert's Appeal*, 85 Penn. St. 84 (1877). In Maryland it is held, that a mere transfer of the certificates of stock without a registry on the corporate book, is incomplete as a gift, and cannot be enforced against the personal representatives of the deceased donor. *Baltimore Retort, &c., Co. v. Mali*, 13 Am. & Eng. Corp. Cas. 49 (1886). But a written memorandum left by a decedent, to the effect that he thereby gives certain stock to a person, but retains the same during life, in order that he, the donor, may have the dividends, is not a valid gift. *Re Shield*, 53 L. T. N. S. 5 (1885).

CHAPTER XIX.

SALES OF STOCK.—COMPETENCY OF PARTIES TO BUY AND SELL STOCK.

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| <p>§ 309-310. (a) Competency of a corporation to purchase shares of its own capital stock.</p> <p>311-312. Rule in the United States.</p> <p>313. Statutory provisions.</p> <p>314. The stock is not merged.</p> <p>315. (b.) Purchase by a corporation of stock in another corporation.—Purchase by railroad.</p> <p>316. Purchases of stock by banks and pledges to banks.</p> <p>317. Purchases of stock by insurance, manufacturing, and other corporations.</p> <p>318. (c.) Infants as purchasers of stock.</p> <p>319. (d.) Married women as purchasers or vendors of stock.</p> <p>320. (e.) Competency of miscellaneous parties.</p> <p>321. (f.) Sales, purchases, and transfers by agents.</p> | <p>§ 322. (g.) Purchases of stock by guardians, executors, and trustees.</p> <p>323. (h.) Sale or pledge of stock by trustee in breach of his trust.</p> <p>324. Liability of trustee.</p> <p>325. Transferee of stock from trustee, transferring in breach of trust, not protected if he take with notice.</p> <p>326. Purchaser with notice that his vendor sells as trustee, may nevertheless be protected.</p> <p>327. Rights and liability of the corporation allowing a transfer by a trustee in breach of his trust.</p> <p>328. (i.) Sales of stock by a guardian.</p> <p>329. (j.) Sales by executor or administrator.</p> <p>330. Duty and liability of the corporation.</p> |
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§ 309. (a.) *Competency of a corporation to purchase shares of its own capital stock.*—In England, a long line of decisions have established the rule that, at common law, a corporation cannot purchase shares of its own capital stock.¹ This rule is "enounced clearly and decisively, and is closely adhered to."² The corporation may be given an express power for this purpose, but unless so given, the purchase is held to be beyond the legal powers of the directors and of the whole body of stockholders.³ The object of

¹ *Re Marseilles Extension Ry. Co., L. R. 7 Ch. 161 (1871)*; *Evans v. Coventry*, 25 L. J. (Ch.) 489, 501 (1856); *Cross's Case*, 38 L. J. (Ch.) 583 (1869); *Morgan's Case*, 1 De G. & Sm. 750 (1849); *Ex parte Morgan*, 1 Mac. & G. 225 (1849); *Eyre's Case*, 31 Beav. 177 (1862). *Cf. Taylor v. Hughes*, 2 J. & Lat. (Irish Ch.) 24 (1844).

² *Zulueta's Claim*, L. R. 5 Ch. 444 (1879), the court saying: "A purchase by a company of their own shares is not a legal transaction, unless there is a clear, distinct, undoubted, and special

authority authorizing them to do so." *Hope v. International Financial Soc., L. R. 4 Ch. Div. 327 (1876)*, holding also that a stockholder may enjoin the purchase. "The law I take to be plain and covered by many decided cases, that it is not competent to a company to take the moneys which have been subscribed for its capital for the purpose of buying up the shares of that company;" distinguishing *Teasdale's Case*, L. R. 9 Ch. 54.

³ *Zulueta's Claim*, *supra*; *Hope v. International Financial Soc., supra*. Under

the rule is, to preserve the rights of the corporate creditors, and also to confine the corporation within the express powers given it, and the implied powers necessary to its transaction of business.¹ If the sale is completed, and the corporation afterwards became insolvent, the stockholder who sold the stock to the corporation is liable, on the winding up, as though he never had made such a sale.² If, however, the stockholder sells to a person, not knowing that the latter is purchasing as a trustee for the corporation, the vendor is not liable on such stock.³ The directors authorizing or directing a purchase for the corporation of shares of its own capital stock, are liable personally to the same extent that the selling stockholder would have been had the sale not taken place.⁴ Generally the transfer is made, not to the corporation directly, but to a trustee on behalf of or for the benefit of the corporation.

an express power to the directors to enter into any contract and engagement that seemed best for the company, such a purchase was upheld. *Singer's Case*, W. N. (1869) 206; *Cockburn's Case*, 4 De G. & Sm. 177 (1850), where power was given by the deed of settlement. See, however, *Ward's Case*, 29 W. R. 768 (1881), where an express power to purchase its own stock was held not to authorize a trafficking in that stock—the buying and selling for purposes of gain.

¹ *Id.* Compare, however, *Ward's Case*, 29 W. R. 768 (1881), where the court says: "If the company could not question it, neither can a creditor, for he can obtain nothing but what the company can get from the shareholders."

² *Walters' 2d Case*, 3 De G. & Sm. 244 (1850); *Richmond's Exrs. Case*, 3 De G. & Sm. 96 (1849); *Munts' Case*, 22 Beav. 55 (1856), where the stockholders disagreed and the corporation bought out one faction; *Daniell's Case*, 22 Beav. 43 (1856); *Bennett's Case*, 5 De G., M. & G. 284 (1854), where the stockholders disagreed concerning the validity of a lease, and the corporation bought out part. If, however, the corporation, six years after the transfer, discovers that the transfer was invalid, and summarily retransfers to the vendor, the latter may apply to a court of equity to compel the corporation to keep the stock. *Gardiner v. Victoria Estates Co.*, 12 Ct. of Ses. (Sc. 4th series), 1356 (1885).

³ *Nicol's Case*, 3 De G. & J., 387 (1858); *Grady's Case*, 1 De G., J. & S.

488 (1863), where the vendee was the managing agent of the corporation, and the sale of the stock was to stop litigation. *Richmond's Case*, 3 De G. & Sm. 96 (1849), holds, however, that if the vendor's selling agent, his solicitor, knew that the sale was for the benefit of the corporation, the stockholder himself is chargeable with knowledge. See *Re Orpen*, 32 L. J. (Ch.) 633 (1863), holding that it is a question for the jury whether the vendee purchased for the corporation or for himself. *Johnson v. Laffin*, 5 Dill. 65; 103 U. S. 800. See also § 251.

⁴ "For every share which they have bought up they are liable to stand in the shoes of the persons whom they may, by buying the shares, have discharged from liability, and to pay up the remainder of the unpaid portion of the capital which these persons would have had to pay if they had not been thus discharged." *Evans v. Coventry*, 25 L. J. (Ch.) 489, 501 (1856). To same effect, *Land Credit Co. of Ireland v. Fermoyle*, L. R. 8 Eq. Cas. 7 (1869); *Marzette's Case*, 42 L. T., N. S. 206 (1880). The directors may have contributions from each other for sums paid out by their authority for such purchases, and for which one or more has been held liable to the corporation. *Ashhurst v. Mason*, L. R. 20 Eq. 225 (1875). The directors are not liable to the vendor of the stock for the failure of the corporation to complete their purchase for it of its own stock. *Abeles v. Cochran*, 22 Kan. 405 (1879).

This practice is not at all necessary, and has no effect, other than a transfer direct to the corporation itself, unless it be that the vendor of the stock may not know that his vendee purchases for the corporation, and thereby escapes liability on the winding up. If the contract is executory, the corporation may repudiate it and refuse to pay the purchase-money for the stock.¹ If, however, the sale is completed, the stock belongs to the corporation, and does not pass to the vendor's assignee in bankruptcy.²

§ 310. Where the transfer of stock to the corporation is made by one of the original subscribers for stock, it frequently becomes a difficult question to decide whether the transaction was a cancellation of the subscription contract or was a sale of the stock to the corporation. Each case turns largely on its own peculiar facts and circumstances. If the transaction is a cancellation, it is legal. In England, if it is a sale, it is illegal. The courts seem to favor a construction whereby the transaction is held to be a sale, and the stockholder made liable on the winding up.³

§ 311. *Rule in the United States.*—In this country the common-law right of the corporation to purchase its own stock is directly the opposite of the English doctrine, and is established by a long line of decisions.⁴ The corporation may not only pur-

¹ The corporation may even refuse to pay the price to the brokers employed by its directors to buy the stock. *Zulueta's Claim*, L. R. 5 Ch. 444 (1879). This, of course, does not authorize the corporation to retain the stock so purchased.

² *Great Eastern Ry. Co. v. Turner*, 42 L. J. (Ch.) 83 (1873).

³ *Hall's Case*, L. R. 5 Ch. 707 (1870), distinguishing *Snell's Case*, L. R. 5 Ch. 22. See also *Thomas' Case*, L. R. 13 Eq. 437 (1872); *Teasdale's Case*, L. R. 9 Ch. 54 (1873); *Duke's Case*, L. R. 1 Ch. Div. 622 (1876).

⁴ The leading case is *City Bank of Columbus v. Bruce*, 17 N. Y. 507 (1858), where a corporation received \$133,000 of its own stock in payment of debts due the corporation, the court saying it is "not aware of any common law principle which forbids it." See also *Verplanck v. Mercantile Ins. Co.*, 1 Edw. Ch. 84 (1831). In the case of *Barton v. Port Jackson & U. F. P. R. Co.*, 17 Barb. 397 (1854), a purchase by a plankroad company of its own stock was held to be against public policy and be-

yond the powers of the directors. In Illinois in *Chicago, P. & Southwestern R. Co. v. President, &c., of Town of Marseilles*, 84 Ill. 145 (1876), the court said "We entertain no doubt that a railroad company may, for legitimate purposes, purchase shares of stock which have been issued to individuals. Such is believed to have been the general custom of such bodies, nor have we known the power to have been questioned." A contract whereby the corporation agreed to take back the stock unless certain things were done within a certain time, was sustained. s. c. Id. 643, where the court says "the power of the directors of a company, when not prohibited by their charter to purchase shares of stock of their company," is well recognized. *Clapp v. Peterson*, 104 Ill. 26 (1882); *Chetlain v. Republic Life Ins. Co.*, 86 Ill. 220 (1877); *Fraser v. Ritchie*, 8 Bradw. 554 (1881), where a perfectly solvent concern sold certain property and took its own stock in payment. *Dupre v. Boston Water Power Co.*, 114 Mass. 37 (1873),

chase shares of its own capital stock, but may take them in pledge or mortgage. The purchase may be by authority of the directors, and need not be authorized by the stockholders in meeting assembled. In Illinois and Massachusetts this doctrine is enounced clearly and explicitly. In Kansas, on the other hand, a contrary doctrine is sustained, and the English rule is adopted in its integrity.¹

the court saying: "In the absence of legislative provision to the contrary, a corporation may hold and sell its own stock, and may receive it in pledge or in payment in the lawful exercise of its corporate powers." *Leland v. Hayden*, 102 Mass. 542 (1869); *Crease v. Babcock*, 51 Mass. 525, 557 (1846), holding that the stockholders are not liable for the deficiency caused by part of the stock being owned by the corporation. In Pennsylvania, in *Eby v. Guest*, 94 Penn. St. 160 (1880), and *Early & Lane's Appeal*, 89 Id. 411 (1879), it was held that "the assignment of the stock of a corporation to itself, as collateral security for a loan, divests the title of the assignor so far as to prevent a sale of it under a *fi. fa.* against the assignor." But in *Coleman v. Columbia Oil Co.*, 51 Penn. St. 74 (1865), where a stockholder had accepted the benefit of the purchase, and then objected to its legality, the court said: "The employment of corporate funds to speculate in the stock of the company to which the funds belong, is not a practice to be encouraged, but the present plaintiff is not in position to censure the practice." He "should have sought an injunction against the company to restrain the purchase, or to cancel it if done before he had knowledge of it; or if he would bring an action at law he should have declared for his share of the funds which he complains were misapplied in buying the shares." In Ohio the early case, *Taylor v. Miami Ex. Co.*, 6 Ohio Rep. 176 (1833), held that a bank may receive from the stockholders transfers of stock in payment of debts previously contracted by them. See also *State of Ohio v. Franklin Bank of Columbus*, 10 Ohio Rep. 91, 97 (1840). But in *Cappin v. Greenlees*, 38 O. St. 275 (1882), the court refused to enforce an executory contract for the sale to the corporation of its own stock, and said: "The doctrine that corporations, when not prohibited by their charters, may buy and sell their own stock, is supported by a line of authorities. . . . But, never-

theless, we think the decided weight of authority, both in England and in the United States, is against the existence of the power, unless conferred by express grant or clear implication. The foundation principle upon which these latter cases rest is that a corporation possesses no powers except such as are conferred upon it by its charter, either by express grant or necessary implication." The proposed purchase was held to be invalid under the constitutional provision imposing a personal liability on all stockholders. In Georgia, in the case *Hartridge v. Rockwell*, R. M. Charlton, 280 (1826), the court held: "If from the course of business or the state of things the capital of the bank cannot be usefully employed in loans, there can, I think, be no objection against the purchase of its own stock." The legislature, however, thought differently, and by the Penal Code of 1833 made such purchases a penal offense. See *Robinson v. Beale*, 26 Ga. 17 (1858), where the purchase was held to be authorized under a power to purchase goods, &c. See also, as supporting the doctrine, *Farmers & Mechanics Bank v. Champlain Transportation Co.*, 18 Vt. 131, 139 (1846); *Iowa Lumber Co. v. Foster*, 49 Iowa, 25 (1878), under a power to purchase "property that may be deemed desirable in the transaction of its business." *State Bank of Ohio v. Fox*, 3 Blatchf. 431 (1856), where the stock was taken in payment of a debt due the corporation. *Of. Re Republic Ins. Co.*, 3 Biss. 452, 457 (1873). Compare also *Thompson on Liability of Stockholders*, §§ 234, 242.

¹ *German Sav. Bank v. Wulfekuhler*, 19 Kan. 60 (1877), holding that a bank cannot purchase its own stock, except in a few cases for the purpose of securing some previously existing debt. By so doing the bank "might reduce the amount of its capital stock below the amount required by law, and might also impair or even destroy all security given by law to the creditors of the bank." Person sell-

A corporation may take its own stock by way of gift¹ or bequest.²

§ 312. The difference between the English and American doctrine is largely due to the fact that in England corporate creditors have no greater rights than the corporation has, and hence would be liable to an unreasonable risk if the corporation could purchase shares of its own capital stock. In this country the familiar principle that the capital stock is a trust fund for the benefit of creditors obviates this objection to a purchase by a corporation of its own stock. In Illinois, the State where the rights of the corporation to make such purchases is most clearly and decisively established, the collateral principle that such purchases are to be declared illegal and voidable at the instance of corporate creditors, who are injured thereby, is distinctly stated and rigidly applied.³ If the corporation is insolvent at the time of the purchase, it is clearly an invalid transaction, and will be set aside.⁴ The better rule goes still further, and declares that if a corporation, by a purchase of shares of its own capital stock, thereby reduces its actual assets below its capital stock, or if the actual assets at that time are less than the capital stock, such purchase may be impeached and set aside, and the vendor of the stock rendered liable thereon at the instance of a corporate creditor.⁵ Such a

ing the stock to the bank is liable to it for the price received, even though he used an intermediate dummy in the transfer. The corporation may contract, at the time of issuing its stock, to purchase it at any time from the holder. *Bent v. Hart*, 10 Mo. App. 143 (1881).

¹ *Lake Superior Iron Co. v. Drexel*, 90 N. Y. 87, where its legality was assumed.

² *Rivanna Nav. Co. v. Dawsons*, 3 Gratt. 19 (1846).

³ *Clapp v. Peterson*, 104 Ill. 26 (1882); *Peterson v. Ill. Land & Loan Co.*, 6 Bradw. 257 (1880). In *Crandall v. Lincoln*, 52 Conn. 78 (1884), where stock was bought for the corporation by a corporate agent, the latter was held liable to the receiver of the corporation for the money so expended. The court said: "The statute forbidding the company to make dividends payable from the stock, and to loan money upon a pledge of its stock, by necessary implication forbids the company from purchasing its stock. . . . As a rule, to which there are few, if any, ex-

ceptions, when a stockholder conveys his stock to the company, and receives in return a portion of the capital, he holds the money so received subject to the superior equities of creditors." But the selling stockholder, not knowing that his vendee buys for the corporation, is not liable. *Johnson v. Laffin*, 5 Dill. 65; 103 U. S. 800.

⁴ *Currier v. Lebanon Slate Co.*, 56 N. H. 262 (1875).

⁵ *Fraser v. Ritchie*, 8 Bradw. (Ill.) 554 (1881), holding that the right of the corporation to purchase its own stock is subject to certain restrictions, "one of which is that it shall not be done at such time and in such manner as to take away the security upon which the creditors of the corporation have the right to rely for the payment of their claims; or, in other words, so as not to diminish the fund created for their benefit. Each case must, therefore, depend upon and be determined by its own facts and circumstances." *Gillett v. Moody*, 3 N. Y. 479 (1850).

rule would go far towards reconciling the decisions in this country.

§ 313. *Statutory provisions.*—Frequently statutes are passed expressly prohibiting a corporation from purchasing shares of its own stock.¹ The national banks in this country are prohibited from so doing by the statutes of the Federal government.² In New York, by statute, both moneyed³ and railroad⁴ corporations are prohibited from purchasing shares of their own capital stock, except that moneyed corporations are, by implication, allowed to invest their surplus profits in such purchases.

§ 314. *The stock is not merged.*—When a corporation buys shares of its own capital stock, the capital stock is not reduced by

¹ General Statutes of Colorado (1883), p. 189, § 35; p. 183, § 10. In Pennsylvania, on the other hand, the corporation may, with the approval of the stockholders, "invest the surplus or other funds or earnings" in the purchase of shares of its own capital stock.

² R. S. of U. S. § 5201. "No association shall make any loan or discount on the security of the shares of its own capital stock, nor be the purchaser or holder of any such shares, unless such security or purchase shall be necessary to prevent loss upon a debt previously contracted in good faith, and stock so purchased or acquired shall within six months from the time of its purchase be sold or disposed of at public or private sale, or in default thereof a receiver may be appointed to close up the business of the association." See *Johnson v. Laffin*, 5 Dill. 65; 103 U. S. 800; holding that if a stockholder in good faith and without notice sells his stock to one who purchases for the bank, the sale is valid so far as he is concerned and he is not liable thereon. See also *Bank v. Lanier*, 11 Wall. 369 (1870).

When the president of the bank buys its stock for the bank itself, taking title in his own name, he is liable as a stockholder. The purchase for the bank, however, is void. *Bundy v. Jackson*, 24 Fed. Rep. 628 (1885). Although a national bank must sell its stock taken in payment of a debt within six months, it may sell on credit, taking a note in payment and the stock as collateral. *Union Nat'l Bank v. Hunt*, 76 Mo. 439 (1882). Where a national bank receives its own stock in pledge at the time of making the loan, and sells the stock as collateral, on failure of the debtor to pay, the latter

cannot complain that the statute has been violated. *Nat'l Bank of Xenia v. Stewart*, 107 U. S. 676 (1882). See also *Gold Mining Co. v. National Bank*, 96 U. S. 640, (1877); *Shoemaker v. Nat. Mechanics' Bank*, 31 Md. 396; *O'Hare v. Second Nat. Bk.*, 77 Penn. St. 96; *Stewart v. Nat. Union Bank*, 2 Abb. (N. S.) 424 (1869). A national bank president and directors are not liable criminally for purchasing the stock of the bank for the bank itself. *United States v. Britton*, 107 U. S. 192 (1882); *Id.* 108 U. S. 655 (1882).

³ 1 R. S. ch. 18, title 2, art. 1, § 1 (5) (p. 1367, 7th ed.). "The evident intention was, to prohibit a division of the capital, of any portion of it, among the stockholders, by whatever instrumentality the powers of the corporation in doing the act might be exerted." *Gillet v. Moody*, 3 N. Y. 479, 487. See also *U. S. Trust Co. v. U. S. Fire Ins. Co.*, 18 N. Y. 199, 226 (1858). But purchasers of the stock from a banking corporation that had purchased it in violation of the statute cannot complain. They cannot impeach their own title. *Case of the Reciprocity Bank*, 22 N. Y. 9, 17 (1860). Nor can the vendor of the stock to the bank claim that the sale was invalid. He is estopped. *United States Trust Co. v. Harris*, 2 Bosw. 75, 91 (1857).

⁴ N. Y. Session Laws, 1850, ch. 140 § 8 (p. 1547, 7th ed. of R. S.), the statute reading "It shall not be lawful for such company to use any of its funds in the purchase of any stock in its own, or in any other corporation." *Id.*, Laws 1881, ch. 468, § 12, with the addition "except so far as the same may be agreed upon in its articles of association," in cases of certain railroad corporations.

that amount, nor is the stock merged.¹ So long, however, as the corporation retains the ownership, the stock is lifeless, without rights or powers. It cannot be voted nor can it draw dividends, even though it is held in the name of a trustee for the benefit of the corporation.² But at any time the corporation may resuscitate it by selling it, and transferring it to the purchaser. Such sale may be made upon the authority of the corporate directors.³ It may be sold at its market value, and need not be held for its par value, as is necessary in an original issue of stock.⁴

§ 315. (b.) *Purchase by a corporation of stock in another corporation.—Purchase by railroad.*—It may be stated as a general rule, with but few exceptions, that a corporation has no implied power to purchase shares of the capital stock of another corporation. Especially is this the rule as regards railroad corporations.⁵ It has been firmly settled by well-considered cases that one railroad company cannot purchase shares of stock in another railroad company, especially where the purchase is for purpose of controlling or absorbing the latter.⁶ In a few in-

¹ *State v. Smith*, 48 Vt. 266 (1876); *Williams v. Savage Mfg. Co.*, 3 Md. Ch. 418, 451 (1851); *City Bk. of Columbus v. Bruce*, 17 N. Y. 507 (1858); *State Bank of Ohio v. Fox*, 3 Blatchf. 431 (1856), the court saying: "The stock was not extinguished or destroyed by the purchase thereof by the corporation." *Vail v. Hamilton*, 85 N. Y. 453 (1881); *American Ry. Frog Co. v. Haven*, 101 Mass. 398 (1869); *Commonwealth v. Boston, &c. R. R. Co.*, 2 New Eng. Rep. 647 (Mass. 1886); *Ex parte Holmes*, 5 Cow. 426 (1826). See also § 282.

² See Chap. XXXVIII.

³ *State Bank of Ohio v. Fox*, 3 Blatchf. 431 (1856); *State v. Smith*, 48 Vt. 266 (1876). See also § 282.

⁴ Assumed in *Otter v. Brevoort Petroleum Co.*, 50 Barb. 247 (1867).

⁵ See Green's *Brice's Ultra Vires*, &c. (2d ed.) 91.

⁶ The most important case is *Central R. R. Co. v. Collins*, 40 Ga. 582 (1869), where a stockholder in one railroad obtained an injunction against its purchase for purposes of consolidation, of stock in a rival and competing railroad. The court declared the purchase to be beyond the corporate powers and contrary to public policy, and says "it is a general principle that a railroad company, with-

out express authority given by the legislature to make the purchase, cannot purchase stock in another railroad company." *Angell & Ames*, § 392. To same effect, *Hazelhurst v. Savannah, G. & N. A. R. R. Co.*, 43 Ga. 13, 57 (1871), the court saying: "If one railroad may, at its option, buy the stock of another, it practically undertakes a new enterprise not contemplated by its charter. This it cannot do by any implication. The power so to do must be clear." In the case *Elkins v. Camden & Atlantic R. R. Co.*, 36 New Jersey Eq. R. 5 (1882), a similar injunction was granted. Such purchase is not authorized by a power to lease other lines, nor to build them. "The purchase of a rival railroad is (not to speak of public policy) foreign to the objects for which the defendant was incorporated. . . . As a purchase with a view to extinguishing competition, the transaction is clearly *ultra vires*." It is immaterial that the complainant purchased stock for the purpose of obtaining the injunction. *Salomons v. Laing*, 12 Beav. 339, 353 (1850); *Great Northern Ry. Co. v. Eastern Counties Ry. Co.*, 21 L. J. (Ch.) 837 (1851), where the object was to control the corporation. The court said it was an "attempt to carry into effect, without the intervention of Parliament, what cannot lawfully be

stances, particular corporations, by their charters, are given the power to invest in other railroad stocks, and in other instances general statutes to that effect prevail.¹ In New York, on the other hand, such purchases are prohibited by statute, excepting by corporations to build railroads in foreign countries.² In other States also, such purchases are prohibited by statute.³ In Kansas it is

done except by Parliament, in the exercise of its discretion with reference to the interest of the public. *Maunsell v. Midland, Great Western Ry. Co.*, 1 Hem. & M. 130 (1863), relative to the power of a railroad company to subscribe for the stock of another railroad. *Central R. R. Co. of N. J. v. Pennsylvania R. R. Co.*, 31 N. J. Eq. Rep. 475, 494 (1879), where the defendant was enjoined from building another railroad, by means of an independent corporation operated by dummies. The court said: "A corporation cannot in its own name subscribe for stock or be a corporation under the general railroad law, nor can it do so by a simulated compliance with the provisions of the law through its agents as pretended corporators and subscribers for stock." *Pearson v. Concord R. R. Co.* (New Hampshire Supr. Ct. Aug. 30, 1883), where a railroad had purchased a controlling interest in the stock of a connecting railroad and was managing it in the interest of the former road. A suit by a stockholder of the defrauded road to enjoin such acts was sustained. The court said: "It can no more make a permanent investment of funds in the stock of another road, than it can engage in a general banking, manufacturing, or steamboat business. It is neither incidental to the purposes of its incorporation, nor necessary in the exercise of the powers conferred by its charter. If it can purchase any portion of the capital stock of the Concord road, why may it not buy up all the stock of the latter corporation, and thus engage in the business for which its charter gives it no authority? And what would hinder a banking corporation from becoming a manufacturing company, or a manufacturing company from becoming a railroad corporation." See also § 60. *Cf. Great Western Ry. Co. v. Metropolitan Ry. Co.*, 32 L. J. (Ch.) 382 (1863). Where a railroad company, in the name of one of its leased lines, contracted to purchase a majority of the stock of still another line, the vendor representing that the last line was unincumbered, the first mentioned company may

avoid the contract by proving that an incumbrance rested on the road to be sold. *Southwestern Ry. Co. v. Papot*, 67 Ga. 675 (1881). The rule, above stated, does not prevent a controlling stockholder in one railroad corporation from becoming the controlling stockholder in another railroad corporation. *Havemeyer v. Havemeyer*, 43 Super. Ct. (N. Y.) 506; 45 Id. 464; aff'd, 86 N. Y. 618; *O'Brien v. Breitenbach*, 1 Hilt. 304.

¹ Thus by ch. 276, Laws 1836 of Maryland, the Baltimore & Ohio R. R. Co. was authorized to *subscribe* to the stock of other railroads to a specified extent. See *Mayor v. Baltimore & Ohio R. R. Co.*, 21 Md. 50 (1863). In Ohio the Revised Statutes (1880) provide that "any [railroad] company may aid another in the construction of its road, by means of subscription to the capital stock of such company or otherwise for the purpose of forming a connection of the roads of the companies, when the road of the company so aided does not form a competing line," (taken from Act of March 3rd, 1851, § 4). See *Zabriski v. Cleveland, C. & C. R. Co.*, 23 How. 381 (1859). The case *White v. Syracuse & Utica R. R. Co.*, 14 Barb. 559 (1853), held to be constitutional and valid, a general law allowing any New York railroad to *subscribe* to the stock of the Great Western R. R., Canada West.

² New York Session Laws 1850, § 140, § 8; Laws 1881, ch. 468, § 12, as to railroad corporations. If one road has been leased to another, the latter may exchange its stock for stock in the former. N. Y. Session Laws 1867, ch. 254, as am'd by Laws 1879, ch. 503.

³ In Pennsylvania the statute prohibits any corporation from using "its funds in the purchase of any stock in any other corporation, or to hold the same, except as collateral security for a prior indebtedness." *Brightley's Digest*, vol. 1, p. 343, § 30. So also General Statutes of Colorado (1883), p. 183, § 10 and p. 189, § 35; Code of Tenn. (1884), § 2496; Indiana R. S. (1881), 3858. See 8 Southern Law Rev. 369.

held that a railroad company may purchase stock in a connecting company with a view to consolidation.¹

§ 316. *Purchases of stock by banks and pledges to banks.*—A banking corporation has at common law no power to purchase or invest in the stock of another corporation, whether that other corporation be itself a bank or of a different business.² The bank is organized for the purpose of receiving deposits, and loaning money, not for the purpose of dealing in stocks. Any attempt to engage in such transactions is a violation of its charter rights, and of its duty towards the stockholders and the public. There is a difference of opinion as to whether a pledge of stock, as collateral security for a loan made by the bank at the time of pledging the stock, is legal. The weight of authority holds that such a pledge of stock is valid and may be enforced.³ This rule is in accordance with a widespread custom of banks, and seems to have been denied in but one case. As regards a pledge of stock to a

¹ *Ryan v. Leavenworth, A. & N. W. Ry. Co.*, 21 Kan. 365 (1879). The court said: "Neither the interests of the public nor the interests of the companies would be sacrificed or prejudiced necessarily, if the roads were operated under one management, or if the two companies were consolidated upon equitable terms, so as to form a continuous line of railroad."

² *Talmage v. Pell*, 7 N. Y. 328, 347 (1852), the court saying that banks "have no power to purchase State or other stocks, for the purpose of selling them at a profit, or as a means of raising money, except where such stocks have been received in good faith, as security for a loan made by, or a debt due to such association, or where taken in payment, in whole or in part, of such loan or debt." *Nassau Bank v. Jones*, 95 N. Y. 115, 120 (1854). "It is scarcely conceivable that it can be seriously urged that a moneyed corporation, having under its charter the right to transact a banking business only, may legally engage, as a corporation, in the construction of railroads, or in furnishing money for such an object, in exchange for the stock of a railroad corporation." *First Natl. Bank v. Natl. Exchange Bank*, 92 U. S. 122, 128 (1875), where, in reference to national banks, the court said: "Dealing in stocks is not expressly prohibited, but such a prohibition is implied from the failure to grant the power." *Royal Bank of India's Case*, L. R., 4 Ch. 252 (1869); *Franklin Co. v. Lewiston Institution for Savings*, 68 Me.

43 (1877), the court saying, "it is not within the authority of the trustees of a savings bank, to invest its funds in the stock of manufacturing corporations, unless expressly authorized so to do by its charter or the public laws of the State." The bank is not liable to the corporate creditors on the stock.

³ *Royal Bank of India's Case*, *supra*. "Making advances upon shares in public companies is within the ordinary course of the dealing of bankers." The stock pledged was stock in another bank. To same effect *Re Barned's Banking Co.*, L. R., 3 Ch. 105 (1867); *Shoemaker v. Natl. Mechanics Bank*, 1 Hughes (Ct. Ct. Md.), 101 (1869), as applicable to national banks; also *National Bank v. Case*, 99 U. S. 628 (1878), where the court says: "There is nothing in the argument on behalf of the appellant that the bank was not authorized to make a loan with the stock of another bank pledged as collateral security. That is an ordinary mode of loaning, and there is nothing in the letter or spirit of the National Banking Act that prohibits it. But if there were, the lender could not set up its own violation of law to escape the responsibility resulting from its illegal action." Such a pledge to a national bank is not prohibited by the statute, that the bank shall not take a real estate mortgage as security. So held where the property of the corporation whose stock was pledged consisted of real estate. *Baldwin v. Canfield*, 1 N. W. Rep. 261 (foot paging) (1879). See also *Sistare v. Best*, 88 N. Y. 527.

⁴ *Franklin Bank v. Commercial Bank*,

bank, to secure a debt previously contracted, its legality is unquestioned, and is free from the objections made to a pledge contemporaneous with the loan.¹

§ 317. *Purchases of stock by insurance, manufacturing, and other companies.*—An insurance company has no power or legal right to subscribe for stock in a savings bank and building association;² nor to purchase stock in another insurance company.³ It is difficult to state any rule as regards the right of a manufacturing or trading corporation, to purchase shares of the capital stock of another corporation. It has been held that neither a note selling company,⁴ nor a lumber company,⁵ has power to invest in the shares of a bank; nor a steamship company to subscribe for stock in a dry-dock company.⁶ On the other hand, it has been held that a steamboat company may purchase stock in another rival line, even though the evident purpose be to injure it.⁷ It is clearly legal for a manufacturing corporation to take the stock of another in payment of a debt.⁸ In New York, manufacturing corporations are prohibited by statute, from purchasing stock in any other corporation,⁹ unless such other corporation either produces or consumes the articles in which the former corporation is interested.¹⁰ Religious and charitable and other

36 O. St. 350 (1881), where the legality of the pledge was denied, and the right of the pledgee to have the stock registered in its name not granted.

¹ First National Bank *v.* Natl. Exchange Bank, 92 U. S. 122-128. "In the honest exercise of the power to compromise a doubtful debt owing to a bank, it can hardly be doubted that stocks may be accepted in payment and satisfaction, with a view to their subsequent sale or conversion into money, so as to make good or reduce an anticipated loss."

² Mutual Sav. Bank & Bldg. Assn. *v.* Meriden Agency Co., 24 Conn. 159 (1855), holding the insurance company not liable on the stock.

³ *Re Liquidators of the British Nation Life Assurance Association*, L. R., 8 Ch. Div. 679 (1878), the court refusing to hold the former liable on a winding up, and saying: "The more or less similarity of the objects, or even absolute identity of the objects, does not affect the principle. It is the entering into a new contract of partnership with new persons under a new constitution, which is absolutely *ultra vires* and void, unless specially provided

for and authorized." To same effect *Berry v. Yates*, 24 Barb. 199 (1857).

⁴ Joint Stock Discount Co. *v.* Brown, L. R., 8 Eq. 381 (1869).

⁵ *Sumner v. Marcy*, 3 W. & M. 105 (1847).

⁶ *New Orleans, F. & H. S. Co. v. Ocean Dry-dock Co.*, 28 La. Ann. 173 (1876).

⁷ *Booth v. Robinson*, 55 Md. 419 (1880). This decision goes to the extreme length in allowing one corporation to invest in the stock of another. A manufacturing corporation is not presumed to be incapable of purchasing stock in another corporation. *Parker v. Bernal*, 66 Cal. 112 (1884).

⁸ *Howe v. Boston Carpet Co.*, 82 Mass. 493 (1860).

⁹ As regards New York manufacturing corporations, see Laws 1848, ch. 40, § 8, as changed by Laws 1866, ch. 838, § 3, as amended by Laws 1876, ch. 358, allowing the corporation to purchase stock in other corporations furnishing it with material or taking its finished products.

¹⁰ N. Y. Session Laws, 1848, ch. 40, § 8 (p. 1732, R. S., 7th ed.); 1868, ch. 838 (p. 1743, R. S., 7th ed.), as am'd by Laws 1876, ch. 358.

corporations, not for profit, have, it seems, implied power to invest their funds in stock of other corporations.¹ There has been some controversy, whether one corporation could sell all its property to another corporation, taking pay in stock of the latter, and dividing such stock among the shareholders of the selling corporation. The weight of authority holds that such a transaction is *ultra vires*, and may be prevented by any stockholder of the former corporation.² Where a corporation owns stock in the name of a trustee for the corporation, it is obliged to indemnify such trustee for calls paid by him.³ The stock owned by a corporation may be sold by its general business agent and financial manager and representative, he having apparent power to sell, and the governing body not objecting.⁴

§ 318. (c.) *Infants as purchasers of stock.*—An infant is incompetent to purchase shares of stock. Most cases of this class arise upon a winding up of the corporation, when the infant is placed upon the list of contributories, and in defense infancy is set up.⁵ An infant's purchase of stock is voidable and not void.⁶ This seems to be the rule finally arrived at by the English courts, after some hesitation and difference of opinion. The transfer is similar to a deed which passes an interest to an infant even when coupled with a liability, if it be for his benefit to accept it.⁷ Consequently an infant, upon coming of age, is bound to elect whether he will affirm or disaffirm a purchase of stock made by him while yet an infant.⁸ He may disaffirm, while still

¹ *Pearson v. Concord R. R. Co.* (New Hampshire Sup. Ct., Aug. 30, 1883). "Certain classes of corporations may rightfully invest their moneys in the stock of other corporations, such as religious and charitable corporations, and corporations for literary purposes. The power is not expressly mentioned in their charters, is necessarily implied, for the preservation of the funds with which such institutions are endowed, and to render their funds productive." To same effect *Hodges v. New Eng. Screw Co.*, 1 R. I. 312 (1850).

² *Taylor v. Earle*, 8 Hun, 1 (1876); *Frothingham v. Barney*, 6 Hun, 366. *Contra*, *Treadwell v. Salisbury Mfg. Co.*, 7 Gray, 393; *Hodges v. New England Screw Co.*, 1 R. I. 312 (1850); *Id.*, 3 R. I. 312 (1853). The last case, holding that a court of equity has no juris-

diction to aid a dissenting stockholder in such a case, has been justly criticised and is clearly poor law.

³ *Goodson's Claim*, 28 W. R. 760 (1880).

⁴ *Walker v. Detroit Transit Ry. Co.*, 47 Mich. 338 (1882). See also *Sistare v. Best*, 88 N. Y. 527. That the corporate treasurer may sell the stock, see *Holden v. Metropolitan Natl. Bk.*, 138 Mass. 48.

⁵ See §§ 250, 63.

⁶ *Lumsden's Case*, L. R., 4 Ch. 31 (1868).

⁷ *Id.*

⁸ Where, however, the corporation becomes insolvent just before or just after the infant comes of age, he need not affirm or disaffirm, but may await the action of the corporation. *Mitchell's Case*, L. R., 9 Eq. 363 (1870). Where he is silent for two years after coming of age, and corpo-

an infant, and is then not liable on calls.¹ The plea of infancy is a good defense,² but the plea must allege a disaffirmation within a reasonable time after becoming of age.³ Where a stockholder sells his stock through a stock exchange jobber, and the sale is made to an infant, the jobber is liable to the vendor for calls paid by him in consequence of such infancy.⁴

§ 319. (d.) *Married women as purchasers or vendors of stock.*—At common law, a married woman's rights as regards shares of stock were the same as prevailed with reference to other personal property purchased or owned by her. She had no material rights. Modern statutes have, however, completely changed her rights of property and of contract. These statutes are so different in form and effect, that it is necessary for the purpose of ascertaining the status of a married woman as a stockholder, to consult the statute law of the State of her domicile, and also of the State of the corporation itself.⁵ In England, the severity of the common law has been but partially modified by statute.⁶

rate insolvency then occurs, he is bound. *Idem.* For other cases of ratification, see references in §§ 63, 250.

¹ *Newry & Enniskillen Ry. Co. v. Coombe*, 3 Ex. 565, 578 (1849). "He became a shareholder by contract during infancy, and during infancy he disaffirmed the contract, therefore, in my opinion, he ceased to be a shareholder, liable to be sued for calls."

² *Birkenhead, L. & C. J. Ry. Co. v. Pilcher*, 5 Ex. 24 (1850).

³ *Dublin & Wicklow Ry. Co. v. Black*, 8 Ex. 181 (1852).

⁴ *Nickalls v. Merry, L. R.*, 7 H. L. 530 (1875).

⁵ The wife's capacity to transfer is determined by the law of her domicile. *Hill v. Pine River Bk.*, 45 N. H. 300 (1864); *Dow v. Gould & C. S. M. Co.*, 31 Cal. 629 (1867), holds that in California, a gift of stock from husband to wife is valid, and that after such gift, he could not sell and transfer it as his own. *Leitch v. Wells*, 48 N. Y. 585. The case of *Stanwood v. Stanwood*, 17 Mass. 57 (1820), holds that where the husband does not have the stock transferred to himself on the corporate books, but declares it to be his wife's stock, there is no reduction of it to his possession. See also *Wall v. Tomlinson*, 16 Ves. 413 (1809), to the effect that a transfer of the wife's stock to the husband as trustee, is

not a reduction to possession; also *Arnold v. Ruggles*, 1 R. I. 165 (1837); *Wildman v. Wildman*, 9 Ves. 174 (1803); and *Slaymaker v. Bank of Gettysburg*, 10 Penn. St. 373 (1849), to the effect that only a registry will reduce the wife's stock to the possession of the husband. The wife's stock standing in her name at the time of and after marriage, is not subject to her husband's debts. *Cochrane v. Chambers*, AmbL., 79 n. (1825). *Contra*, *Stamford Bk. v. Ferris*, 17 Conn. 259 (1845). In Connecticut it is held, that the wife is not liable in assumpsit to her husband's creditors, to whom she has pledged her stock, although she subsequently pledges it to another. An express promise to pay on her part is necessary. *Platt v. Hawkins*, 43 Conn. 139 (1875). *Curtis v. Steever*, 36 N. J. Law, 304 (1873), clearly and properly holds that the wife's stock, held by her as her separate estate, is not subject to her husband's debts. See also *Cornell's Case*, 18 W. N. Cases, 289 (Penn. Nov., 1886) and §§ 62, 250, 308.

⁶ By 33 & 34 Vict., c. 93, § 4, married women may purchase or take paid up stock, or stock upon which there can be no liability, but if taken without the consent of her husband, he may apply to the court and have it turned over to himself. Previous to this act, the corporation might refuse to register her as a stock-

§ 320. (e.) *Competency of miscellaneous parties.*—A sale of stock by a person *non compos mentis* is void. The corporation is bound absolutely to know of the lunacy of a transferrer, even though it allows a registry on his ordinary signature and power of sale.¹ An assignee in bankruptcy or for the benefit of creditors, takes only the interest and equitable rights of his assignor. A previous unrecorded transferee of the insolvent's stock is protected.² A partner may accept stock as collateral security for a loan from the firm,³ and may sell and transfer partnership stock.⁴ A director of the corporation itself may buy and sell its stock like any other individual. The information which he has of the affairs of the corporation, whereby he is enabled to buy or sell at an advantage over the person with whom he deals, does not affect the validity of the transaction. He is entitled to the benefit of his facilities for information. There is no confidential relation between him and a stockholder, so far as a sale of the stock between them is concerned, and so long as he remains silent, and does not actively mislead the person with whom he deals, the transaction cannot be set aside for fraud.⁵ A joint owner of stock cannot transfer the interest of the other joint owner where the stock is registered in the name of both.⁶ On the death of one, the survivor takes title to the whole stock.⁷

holder, but now, the corporation must accept her the same as any other applicant for registry. *Regina v. Carnatic Ry. Co.*, 42 L. J. (Q. B.) 169 (1873). Under this act, she may transfer her stock only after it has been formally set aside by statutory authority, as her separate property. *Howard v. Bk. of Eng.*, L. R., 19 Eq. 295 (1875). Where the corporation has allowed a transfer by a married woman, it cannot cancel the registry. *Ward v. South-eastern Ry. Co.*, 2 El. & El. 812 (1860).

¹ *Chew v. Bank of Baltimore*, 14 Md. 299 (1859).

² *Dickinson v. Central Natl. Bk.* 129 Mass. 279 (1880); *Purchase v. New York Exchange Bank*, 3 Rob. (N. Y.) 164 (1865). *Contra*, *Shipman v. Ætna Ins. Co.*, 29 Conn. 245 (1860), where the previous transferee delayed unreasonably in claiming ownership of the stock.

³ *Weikersheim's Case*, L. R., 8 Ch. 831 (1873). In *Comstock v. Buchanan*, 57 Barb. 127 (1864), however, where the stock was registered in both partners' names, a contrary rule was upheld.

⁴ *Quiver v. Marblehead Social Ins.*

Co., 10 Mass. 476 (1813). Cf. *Sargent v. Franklin Ins. Co.*, 8 Pick. 90 (1829).

⁵ *Board of Com'rs of T. County v. Reynolds*, 44 Ind. 509 (1873); *Carpenter v. Danforth*, 52 Barb. 581 (1868). This case was disapproved by the commentator to Story's Eq. Juris. 12th ed., 229, n., but the disapproval is omitted in the 13th ed. So also *Grant v. Attrill*, 11 Fed. Rep. 469 (1882), where the sale was induced by threat of assessments. See also *Johnson v. Laffin*, 5 Dill. 65, 83 (1878); *Jones v. Alley* (U. S. Ct. Ct. Ill., July 18th, 1886); *Gilbert's Case*, L. R., 5 Ch. 559 (1870). See also *Heman v. Britton*, 14 Mo. (App.) 109; *aff'd* 84 Mo. 657.

⁶ *Standing v. Bowring*, L. R., 27 Ch. D. 341 (1884); *Comstock v. Buchanan*, 57 Barb. 127 (1864). But if the other joint-owner dies first, the previous transfer of the survivor is effective and conveys the whole. *Slaymaker v. Bank of Gettysburg*, 10 Penn. St. 373 (1849).

⁷ *Garrick v. Taylor*, 3 L. T. (N. S.) 460 (1860); *Hill's Case*, L. R., 20 Eq. 583 (1874).

§ 321. (*f.*) *Sales, purchases, and transfers by agents.*—Where stock is purchased by one person in his own name by due authority for himself and another, the latter is a part owner, and has rights and liabilities as such.¹ The Statute of Frauds does not apply to such an arrangement.² Stock may be purchased by an agent, and in making such a purchase the agent is not permitted to make a secret profit, even though he acts without compensation.³ A *bona fide* purchaser for value, and without notice of stock from a vendor who delivers the certificates therefor indorsed in blank by another, or indorsed by the vendor himself, is protected and entitled to the stock, although it afterwards transpires that the agent was selling as agent of another and had been guilty of a breach of trust.⁴ But the transferee is not protected where he is not a *bona fide* purchaser.⁵ Where the same person acts as agent for both the transferrer and the transferee, and ab-

¹ *Stover v. Flack*, 41 Barb. 162 (1862).

² See Ch. XX.

³ *Kimber v. Barber*, L. R. 8 Ch. 56 (1872), holding that where a person offers to buy for another, stock at a certain price, but buys it at a less price and keeps the difference, he is liable to the vendee for his gains.

⁴ *Honold v. Meyer*, 36 La. Ann. 585 (1884); *Strange v. Houston & T. C. R. R. Co.*, 53 Tex. 162 (1880); *Dovey's Appeal*, 97 Penn. St. 153 (1881), and see many cases in Chapter on Stock Brokers, where this principle of law is often involved. The case of *Taylor v. Great, &c., R. R. Co.*, 4 De G. & J., 559, to the contrary, turns on the English doctrine that transfers in blank are not valid. The case of *Donaldson v. Gillet*, L. R. 3 Eq. 274 (1866), where the pledgee of one who held the certificate indorsed to himself was not protected, since the pledgor had purchased as agent and had fraudulently taken title in his own name, would not be good law in this country, where the failure to have the transfer registered has no effect on the pledgee's rights under such circumstances. The case of *McNeil v. Tenth National Bank*, 46 N. Y. 325 (1871), is not only the leading case on the stoppel of the principal from repudiating the sale or pledge of his stock by his agent, whom he intrusted with the certificates indorsed in blank, but it is one of the leading cases on the law of the *quasi* negotiability of stock. *Rumball v. Metropolitan Bank*, L. R. 2 Q. B. D. 194 (1877), where a broker committed a

breach of trust. The court said the stockholder "is in the position of a person who has made a representation, on the face of his scrip, that it would pass with a good title to any one on his taking it in good faith and for value, and who has put it in the power of his agent to hand over the scrip with this representation to those who are induced to alter their position on the faith of the representation so made." *Moodie v. Seventh Nat'l Bk.*, 3 Weekly N. C. 118 (1876), holding that if the purchaser takes partly for an antecedent debt he is not a *bona fide* holder to that extent. *Dovey's Appeal*, 97 Penn. St. 153 (1881). An assignee in insolvency of the agent does not take the stock. See § 320. An agent to collect dividends who loans the stock at a profit, is liable for its loss, even though he informed the owner of the loan, and she did not object. *Persch v. Quiggle*, 57 Penn. St. 247 (1868). A *bona fide* purchaser from the agent is protected. *State Bk. v. Cox*, 11 Rich. Eq. 344 (1860); *West, &c., Co.'s Appeal*, 81 Penn. St. 19 (1870); *Otis v. Gardner*, 105 Ill. 436 (1883); *Gulick v. Markham*, 6 Daly, 129 (1875); *Martin v. Sedgwick*, 9 Beav. 333 (1846); *Appeal of Lionard*, 6 East. Rep. 877 (Penn. 1886).

⁵ *Talmage v. Third Nat'l Bk.* 91 N. Y. 531 (1883); *Crocker v. Crocker*, 81 N. Y. 507 (1865); *Weaver v. Borden*, 49 N. Y. 286 (1872), where the agent fraudulently bought in his own name and then fraudulently sold.

sconds with the purchase price after the certificates have been delivered, but before registry on the corporate books, the transferee is protected.¹ An agent's power to sell stock does not authorize him to pledge it.²

A person who knows or has the means of knowing that another person holds stock as an agent only, cannot take such stock in pledge from the agent, although the latter represents that the money is to be used for his principal. The principal may recover the stock if he has not authorized the pledge.³ The real owner of stock may compel the nominal owner to transfer the stock to him.⁴ The corporation may disregard the nominal holder and allow the real owner to sell and transfer the stock.⁵ Where the corporation knows that the vendor is selling as the agent of the stockholder, who has given to the agent the certificates indorsed in blank, it must see to it that the agent has full power to sell the stock and is liable for allowing a registry where the agent has not such power.⁶

§ 322 (*g.*) *Purchases of stock by guardians, executors, and trustees.*—In England, at an early day, the common law rule was declared to be that guardians, executors, and trustees had no right to invest the trustee fund in the stocks of private corporations, and that if they did so they themselves were personally liable for the moneys so invested.⁷ The rigor of this rule has been relaxed somewhat in England, by statute and by orders in chancery, so that such investments may be made in the stock of the banks of England and of Ireland and the East India Company.⁸ In this country, aside from a few *dicta* and a few decisions to the contrary, the English rule, in its original integrity, is upheld and fol-

¹ *Ex parte Shaw*, L. R. 2 Q. B. D. 463 (1877).

² *Merchants Bk. of Canada v. Livingston*, 74 N. Y. 228 (1878).

³ *Fisher v. Brown*, 104 Mass. 259 (1870).

⁴ *Colquhoun v. Courtenay*, 43 L. J. (Ch.) 388 (1874).

⁵ *Sabin v. Bank of Woodstock*, 21 Vt. 353 (1849), holding also that the nominal holder is not protected, although he subsequently becomes the real owner of the stock.

⁶ *Woodhouse v. Crescent Mutual Ins. Co.*, 35 La. Ann. 238 (1882), holding also that the transferee, who is charged with

receiving with notice, may be joined as a party defendant.

⁷ *Trafford v. Boehm*, 3 Atk. 440 (1746), where the investment was in bank and South Sea stock. Lewis on Trusts, 281 (7th ed. 1879), says that "unless specially given power, it is settled in England that a trustee may not invest the trust fund in the stock of any private company, as South Sea stock, bank stock, &c., for the capital depends upon the management of governors and directors, and is subject to loss."

⁸ Lord St. Vincent's Act, 22 & 23 Vict. ch. 35, § 32; 23 & 24 Vict. ch. 38.

lowed. The weight of authority clearly holds that the investment of trust funds in the stock of railroad, insurance, bank, manufacturing, or other corporations, are made at the peril of the trustees.¹ The *cestui que trust* may hold the trustee liable for the amounts so invested, together with interest upon the same. Where the trustee is authorized to purchase stock he is not liable for the embezzlements of an agent whom, with due care, he employs to make the purchase.²

§ 323. (h.) *Sale or pledge of stock by trustee in breach of his trust.*—It is the function and duty of a trustee to keep and preserve the trust property, and to apply the income according to

¹ In New York the case of *King v. Talbot*, 40 N. Y. 76 (1869), aff'g 50 Barb. 453, clearly enounces and sustains this rule. The court said: "The moment the fund is invested in bank, or insurance, or railroad stock, it has left the control of the trustees; its safety and the hazard, or risk of loss, is no longer dependent upon their skill, care, or discretion, in its custody or management, and the terms of the investment do not contemplate that it ever will be returned to the trustees. . . . The fund has been voluntarily placed in a condition of uncertainty, dependent upon two contingencies: First, the practicability of making the business profitable, and, second, the judgment, skill and fidelity of those who have the management of it for that purpose." *Adair v. Brimmer*, 74 N. Y. 539, 551 (1878), where the trustees were held liable for selling coal lands, taking in pay coal stocks, they being authorized by the will to invest in such securities as they deemed safe. *Mills v. Hoffman*, 26 Hun, 594 (1882); reversed in 92 N. Y. 181, but not on this point. *Ackerman v. Emott*, 4 Barb. 626 (1848). See also *Berry v. Yates*, 24 Barb. 210; *Brown v. Campbell*, Hopkins Ch. (2d ed.) 265 (1824). In Pennsylvania the rule is the same. *Nyce's Appeal*, 5 Watts & Serg. 254 (1843), holding the trustee liable for investment in United States bank stock, although the guardian approved of the trustee's investment. *Norris v. Wallace*, 3 Penn. St. 319 (1846), where the investment was in the stock of a suspended bank. *Worrell's Appeal*, 9 Penn. St. 508 (1848); navigation stock not good, although dividends had been accepted by the *cestui que trust*; sustained on 2d appeal, 23 Penn. St. (1854). *Rush's Estate*, 12 Penn. St. 375 (1849), stock in Lehigh Coal and Nav. Co. not good.

Hemphill's Appeal, 18 Penn. St. 303 (1852), United States bank stock not good. *Pray's Appeal*, 34 Penn. St. 100 (1859), manufacturing corporation stock not good, the works being unfinished. *Barton's Estate*, 1 Pars. 24, doubted. *Ihmsen's Appeal*, 43 Penn. St. 431 (1862), railroad stock not good. In New Jersey the rule is the same. *Gray v. Fox*, 1 N. J. Eq. Rep. 259 (1831); *Halsted v. Meekers, Exrs.* 18 N. J. Eq. Rep. 136 (1866); *Ward v. Kitchen*, 30 N. J. Eq. Rep. 31 (1878). Also in New Hampshire. *Kimball v. Redding*, 31 N. H. 352 (1855), stock in contemplated railroad not good. *French v. Currier*, 47 N. H. 88, 99 (1866), unproductive stock not good. In Massachusetts the tendency is to favor a contrary rule, although no case seems to have clearly decided that such investments are legal. In the case of *Harvard College v. Amory*, 26 Mass. 446 (1830), express power was given. In *Lovell v. Minot*, 37 Mass. 116 (1838), the stock was taken as security. *Kinmouth v. Brigham*, 87 Mass. 270, and *Brown v. French*, 125 Mass. 410, were not cases of investment in stocks. Several of the Southern States clearly uphold the rule that trustees, &c., may invest the trust funds in stocks. *Boggs v. Adger*, 4 Rich. Eq. (S. C.) 408 (1852), United States bank stock good. *Washington v. Emory*, 4 Jones' Eq. (N. C.) 32 (1858), railroad stock good. *Gray v. Lynch*, 8 Gill (Md.), 403 (1849), bank stock good. *Smyth v. Burns*, 25 Miss. 422 (1853), bank stock good. *Lamar v. Micou*, 112 U. S. 452 (1884), and 114 U. S. 218 (speaking for Georgia and Alabama), bank and railroad stock good, but not Confederate bonds. See also on this subject, generally, 40 Am. Dec. 515, notes.

² *Speight v. Gaunt*, L.R. 9 App. Cases, 1 (1883).

the terms of the instrument creating the trust. As a general rule it is not his duty or his right to sell or change the investment. Unless the instrument creating the trust authorizes the sale of the trust property, it is a breach of trust for the trustee to make a sale. In this respect the powers of a trustee differ widely from those of an executor or administrator, and the rule applies to a trustee holding in trust shares of stock.¹ Moreover, under ordinary circumstances, a trustee cannot sell stock held in trust, although such rule be for the purpose of investing the proceeds in other stock or other property.²

§ 324. *Liability of trustee.*—Where a trustee improperly sells shares of stock belonging to the trust estate, the *cestui que trust* has a right to elect to have the stock restored or the amount received for it paid over, together with interest from the time of the sale.³ Were the rule otherwise, in case there was a decline in the value of the stock, the trustee would profit by his own breach of trust. The trust attaches to any stock standing in the name of the trustee, and although the same certificates are not retained, an equal amount of other similar stock owned by the trustee may be applied to the trust.⁴ And in all cases, where the trustee has sold stock belonging to the trust estate in breach of his duties as trustee

¹ Bohlen's Estate, 75 Penn. St. 312 (1874); Bayard v. Farmers & M. Bank, 52 Penn. St. 232 (1866), the court saying: "There is a marked difference between the powers of an administrator or executor, and those of an ordinary trustee. The common duty of the latter is not administration or sale, but custody and management. No purchaser, either of land or personalty, would be safe in buying from a known trustee without looking at the nature and extent of his trust." Jaudon v. National City Bank, 8 Blatchf. 430 (1871), the court saying: "A trustee presumptively holds his trust property for administration and not for a sale." Aff'd, 15 Wall. 165 (1874), where the court says: "The party taking such stock on pledge deals with it at his peril, for there is no presumption of a right to sell it, as there is in the case of an executor. In the former case the property is held for custody, in the latter, for administration. It matters not whether the stock is pledged for an antecedent debt of the trustee or for money lent him at the time. It is unlawful to use it for either purpose."

² Trustee selling stock for purpose of

investing in real estate may be compelled to replace it. Earl Powlet v. Herbert, 1 Ves. 297 (1791). Cf. Bohlen's Estate, 75 Penn. St. 312 (1874). The *cestui que trust* may waive the objection. Duncan v. Jaudan, 15 Wall. 171. The case of Washington v. Emory, 4 Jones' Eq. 32 (1858), holds that a change in the investment is allowable if there is good reason to believe that the estate will be benefited. Trustees should sell the stock if depreciation is probable. Ward v. Kitchen, 30 N. J. Eq. 31 (1878). But not liable for failure to sell if in good faith and sound discretion. Bowker v. Pierce, 130 Mass. 262 (1881). Cannot change stock bequeathed. Murray v. Feinour, 2 Md. Ch. 418 (1851). Nor a good investment to a stock investment. *In re Warde*, 2 Johns. & H. 191 (1861); Waite v. Whorwood, 2 Atkins, 159 (1741).

³ Harrison v. Harris, 2 Atkins, 121 (1740); Bostock v. Blakeney, 2 Brown's Ch. R. 653 (1789); Pocock v. Reddington, 5 Vesey, 800 (1801); Long v. Stewart, 5 Vesey, 809 n. (1801); Hart v. Ten Eyck, 2 Johns. Ch. 62, 117 (1816).

⁴ Pinkett v. Wright, 2 Hare, 120 (1842).

tee, he may be held liable in damages, by the *cestui que trust* or his representative, for the value of the stock.¹

§ 325. *Transferee of stock from trustee, transferring in breach of trust, not protected if he takes with notice.*—A vendee or pledgee of stock, directly from a trustee, is or is not protected in his interest in the stock, according as he is or is not chargeable with notice of the fact that the stock belongs to a trust estate, and that the trustee is using it in breach of his trust. Anything that is sufficient to put a party on inquiry is considered equivalent to actual notice, if inquiry be not made and reasonably satisfied. The law imputes to a purchaser the knowledge of a fact of which the exercise of common prudence and ordinary diligence would have apprized him. This is called constructive notice, and has the same effect as an actual notice of the trusteeship. The most common instance of a constructive notice that stock being sold belongs to a trust estate, is where the words “trustee,” or “in trust,” either with or without the name of the *cestui que trust*, are written on the face of the certificate of stock after the name of the person in whose name it stands on the corporate books. It is well established that such words, indicating a trustee ownership, are notice to the purchaser that his vendor is selling trust property, and that he buys at his peril.² In California, however, it is held, that although the word “trustee” on the face of the certificate, followed by the name of the *cestui que trust*, may give notice that it is trust property, yet that where the word “trustee” is but a cloak for an agency, for the purpose of shielding the real owner from liability on his stock, and from the fact being known that he is dealing in stocks, the court will disregard it, and will not protect him against his agent’s unauthorized sale of the stock.³

¹ This principle of law is assumed in the cases on this subject.

² *Shaw v. Spencer*, 100 Mass. 382 (1868), the court saying that the word “trustee” means trustee for some one whose name is not disclosed, and that a custom of trade disregarding such words on certificates of stock is illegal and ineffectual to protect the purchaser. To same effect, *Jaudon v. National City Bank*, 8 Blatchf. (1871); *aff’d*, 15 Wall. 165, 176, where the court says the purchasers “are chargeable with constructive notice of everything which, upon inquiry, they could have ascertained from the

cestui que trust.” *Gaston v. American Ex. Natl. Bk.* 29 N. J. Eq. Rep. 98 (1878); *Walsh v. Stille*, 2 Parsons’ Sel. Cases in Eq. (Penn.) 17 (1842); *Simons v. Southwestern R. R. Bank*, 5 Rich. Eq. 270 (1853), where a Master in Chancery held the stock in his own name officially. *Loring v. Brodie*, 134 Mass. 453 (1883); *Loring v. Salisbury Mills*, 125 Id. 138 (1878); *Sweeney v. Bk. of Montreal*, 5 Canadian Law Times, 503 (1885).

³ *Brewster v. Sime*, 42 Cal. 139 (1871); *Thompson v. Toland*, 48 Cal. 99 (1874).

There are many other facts which will prevent the vendee from claiming that he is a *bona fide* holder of the stock. Thus, if the stock is pledged by the trustee, who is a director of a bank which is prohibited from loaning to its directors, the bank is not a *bona fide* holder, though without notice or knowledge of the trusteeship.¹

In England, the House of Lords have decided that certificates of stock in railway companies are not negotiable in any respect, and that a transferee of the certificate is not protected until he has obtained registry in the corporate books.² In this country a different rule prevails, and it is accepted and assumed as elementary, that a *bona fide* purchaser for value of stock belonging to a trust estate and sold in breach of trust, is nevertheless protected in his purchase, although he has not registered on the corporate books the transfer. A *bona fide* purchaser through several mesne conveyances, starting from a trustee who sells the stock in breach of trust, is protected.³

§ 326. *Purchaser with notice that his vendor sells as trustee, may nevertheless be protected.*—The mere fact that a purchaser of stock knows he is buying from a trustee, and that the stock belongs to the trust estate, does not put the purchaser to any inquiry beyond ascertaining whether the trustee has power to sell the stock or vary the investment. If he has such power the purchaser will be protected, although the trustee uses the money for his own private purposes, provided the purchaser has no notice of such an intent on the part of the trustee.⁴ The purchaser has a

¹ Albert v. Savings Bk. of Baltimore, 2 Md. 159, 171 (1852).

² Shropshire Union Rys. & Canal Co. v. Queen, L. R., 7 H. L. 496 (1875). Cf. Dodds v. Hills, 2 H. & M. 424 (1865).

³ Salisbury Mills v. Townsend, 109 Mass. 115 (1871); Stinson v. Thornton, 56 Ga. 377 (1876); Cohen v. Grayson, 4 Md. Ch. 357 (1848), where, however, the trustee has been removed by a court, and another trustee appointed, in the State of the corporation, a purchaser of the certificates held by the old trustee is not protected, his purchase being after the removal. Sprague v. Cachigo Mfg. Co., 10 Blatchf. 173 (1872). But in Hal-

brook v. New Jersey Zinc Co., 57 N. Y. 616 (1874), it was held that a successful suit, in a State not the State of the corporation, to remove a trustee, does not affect a *bona fide* purchaser of the certificate from the trustee, the purchase being made pending the suit, and that the corporation allowing registry of the new trustee as holder of the stock, and issuing new certificates to him, is liable in damages to the purchaser from the old trustee.

⁴ Perry on Trusts, § 225, 3d ed. (1882); Lewin on Trusts, 417, 7th ed. (1879); Goddard on Trusts, 125, 127 (1879).

right to assume that the object of the sale is to invest the funds in a permanent investment or to discharge liabilities.¹ Where, however, the purchaser knows that his vendor sells or pledges the stock as trustee, and that the sale or pledge is for the private debts or purposes of the trustee, the purchaser is chargeable with knowledge of the breach of trust, and is not protected.² Nor is a pledgee of stock from a trustee, acting as trustee, protected where the trustee is authorized merely to sell the stock.³ Power to sell does not confer power to pledge.⁴

§ 327. *Rights and liability of the corporation allowing a transfer by a trustee in breach of his trust.*—Where a corporation has notice that a stockholder holds his stock as trustee for another, and the means of ascertaining the character of that trust are within the power of the corporation, it is bound to refuse to allow a registry of the trustee's transfer until it is satisfied that the trustee has power to make the transfer.⁵ If the corporation allows the transfer and the trustee had no power to make it, the corporation is liable to the *cestui que trust*. The fact that the certificate runs to the holder as "trustee" is sufficient notice to the corporation.⁶ Notice to a board of directors is notice to all subsequent boards.⁷ The corporation is bound to see that the sale by the trustee is made in accordance with the terms of the trust. Thus it is liable if it permits a sale and transfer by one trustee when there are two trustees, and a general power of attorney by the other trustee authorizing sales will not

¹ Ashton v. Atlantic Bank, 85 Mass. 217 (1861), where the trustee sold land, took notes in payment and stock as collateral, and sold the notes with the collateral.

² Jaudon v. National City Bank, 8 Blatchf. 430; aff'd, 15 Wall. 165, *sub nom.* Duncan v. Jaudon; Walsh v. Stille, 2 Parson's Sel. Cases in Eq. (Penn.) 17 (1842); White v. Price, 29 Hun, 394 (1886); Simmons v. Southwestern R. R. Bank, 5 Rich. Eq. 279 (1853); Shaw v. Spencer, 100 Mass. 382 (1868), holding also that silence, while the vendee pays an assessment, is no waiver.

³ Loring v. Brodie, 134 Mass. 453 (1883).

⁴ Merchants Bk. of Canada v. Livingston, 74 N. Y. 223 (1878).

⁵ Bayard v. Farmers' & Mechanics' Bk.,

52 Penn. St. 232 (1866), where a refusal of the corporation to transfer until the terms of the trust were examined by its attorney and found to allow the trustee, was sustained. The corporation cannot, however, retain the copies of the probate records used in investigating. Bird v. Chicago, I. & N. R. R. Co., 137 Mass. 428 (1884).

⁶ Loring v. Salisbury Mills, 125 Mass. 188 (1878). See also § 330.

In the case Stockdale v. South Sea Co., Barnardiston's Ch. (folio) 363 (1740), the court said, however, "These great companies are only to consider the person in whose name the stock is standing, unless the trust of that stock is declared in their books."

⁷ Mechanics' Bank of Alex. v. Seton, 1 Pet. 299 (1828).

protect the corporation in its registry of the transfer signed by one.¹ It is liable for allowing a registry of a trustee's transfer when the trust is for an unmarried woman, to take effect when she shall marry.² If there are several *cestui que trustent*, the corporation is liable for allowing one of them to transfer the whole interest in the stock, where by mistake of the corporation the stock had been registered in the name of that one, and not in the name of the trustee.³ If, however, the *cestui que trust* is guilty of laches in taking steps to obtain his rights the corporation is discharged.⁴ The remedy of the *cestui que trust* is in equity, not at law.⁵ A waiver of former breaches of trust is no waiver of the one complained of, and a judgment against the trustee himself is no bar to the suit against the corporation except to the extent that satisfaction has been obtained.⁶ The corporation may be compelled by the court to purchase an equal amount of stock and register it for the benefit of the *cestui que trust*.⁷

§ 328. (i.) *Sales of stock by a guardian*.—At common law a guardian may sell the personal property belonging to him as guardian, without obtaining any special license or authority, and a *bona fide* purchaser from him of such property is protected and is entitled to the property, even though the guardian misappropriates the proceeds of the sale.⁸ This rule applies to shares of stock.⁹ In most of the States, however, statutes have been passed, requiring guardians to obtain the consent of a court, be-

¹ Bohlen's Estate, 75 Penn. St. 312 (1874), nor where the signatures of the other trustees are forged by one. *Cottam v. Eastern Counties Ry. Co.*, 1 J. & H. 243 (1860).

² *Magwood v. R. R. Bk.*, 5 S. C. 379 (1874).

³ *Farmers' & M. Bk. v. Wayman*, 5 Gill (Md.), 336 (1847).

⁴ *Albert v. Sav. Bk. of Baltimore*, 1 Md. Ch. 407 (1849); *aff'd* 2 Md. 159 (1852).

⁵ *Loring v. Salisbury Mills*, 125 Mass. 138 (1878).

⁶ *Id.*

⁷ Bohlen's Estate, *supra*.

⁸ *Field v. Schieffelin*, 7 Johns. Ch. 150 (1823); *Ellis v. Prop. of E. M. Bridge*, 2 Pick. 243 (1824), holding that a *bona fide* purchaser from the guardian of a person *non compos mentis* is protected.

⁹ *Lamar v. Micou*, 112 U. S. 452, 475 (1884), the court saying: "He had the authority, as guardian, without any order of court, to sell personal property of his ward in his own possession, and to reinvest the proceeds." See also *Bank of Va. v. Craig*, 6 Leigh, 399, 432 (1835), to the same effect, and holding that the corporation is not liable for a breach of trust by the guardian in selling the stock. The court said: "If the guardian defrauds his ward, his sureties are responsible; if the purchaser combines in the fraud, he too is chargeable, but the bank cannot interfere and arrest the transfer of its stock by the legal holder of the scrip, upon such pretences. It would trammel and embarrass such transactions, so as to impede materially that transferable character, which is one of the most valuable attributes of stock."

fore selling the personal property of his ward.¹ If such a statutory permission to sell is required, and the vendee of stock has notice that his vendor sells as guardian, the vendee is bound to see that the requisite permission to sell has been given.² An order of the court allowing the guardian to sell is not authority to him to pledge the stock, and the pledgee is bound to take notice of that fact.³ Where stock is sold by a foreign guardian, according to the laws of the State of the guardianship, title passes and the purchaser is protected.⁴

§ 329. (j.) *Sales of stock by an executor or administrator.*—It is the duty of an executor or administrator of an estate to collect the assets, pay the debts, and distribute the remainder according to the provision of the will or of the Statute of Distribution.⁵ In order to pay the debts, the executor may sell the personal property of the estate. Accordingly, the rule has become established that the purchaser of personal property from an executor or administrator is not bound to ascertain whether the sale is necessary in order to pay the debts of the estate, nor to see that the proceeds of the sale are applied to the debts. If he buys in good faith, and for value, he is protected. Such also are the rules applicable to sales of stock by an executor or administrator.⁶ The executors in the State of the decedent may transfer the stock of the estate, and convey a title which the corporation is bound

¹ Mass. R. S. c. 79, § 21.

² *Atkinson v. Atkinson*, 90 Mass. 15 (1864).

³ *Webb v. Graniteville Mfg. Co.*, 11 S. C. 396 (1876).

⁴ *Ross v. Southwestern R. R. Co.*, 53 Ga. 514 (1874).

⁵ *Keylinge's Case*, 1 Eq. Cases, Abr. 239 (1702), holding that where the executor holds the stock for several years, and it declines in value, he is chargeable with its value one year after the death of the testator.

⁶ *Leitch v. Wells*, 48 N. Y. 585 (1872), holding that the *bona fide* transferee is protected, although the executors had previously set aside the same stock to apply to the payment of a certain amount chargeable by the will to the estate annually. *Woods' Appeal*, 92 Penn. St. 379 (1880), holding that a *bona fide* transferee of the executor's transferee is protected, although the latter would not have been, and although the former was aware that

his title came from an executor. The court held that letters of administration are always evidence of power to sell, and that an executorship differed widely from a trusteeship as regards the right to sell. *Prall v. Tilt*, 27 N. J. Eq. 393 (1876); *aff'd*, 28 N. J. Eq. 479 (1877), where the will authorized advances to the sons, and they represented to the transferee that the stock was so advanced to them by the executor. *Lowry v. Commercial & F. Bk. of Baltimore*, Taney (U. S. C. Ct.), 310 (1848). In this case the purchaser had no knowledge or notice that the transferor sold the stock as an executor. *Clark v. South Metropolitan Gas Co.*, 54 L. J. (Ch.) 259 (1885), sustaining a sale of stock by an administratrix of an administrator. *Re London, &c., Tel. Co.*, L. R. 9 Eq. 633 (1870), sustaining the title of a *bona fide* purchaser from the executrix as against an assignee in bankruptcy of the deceased, the assignee having delayed his application for five years.

to recognize, although the corporation itself is domiciled in another State.¹ The rule is otherwise, however, as regards executors appointed in jurisdictions out of the United States.² An executor may pledge estate stock at his bank on a representation that the money is to be used for the estate, and the bank will be protected although the note given by the executor is renewed several times and the proceeds of transaction were passed to the executor's private account.³ So also a *bona fide* purchaser of stock from a life tenant, to whom the administrator improperly transferred it, is protected. The remainderman's remedy is on the administrator's bond.⁴ Where, however, the transferee of the executor knows that the transaction is not for the benefit of the estate, but is a breach of trust, he is not protected.⁵ Frequently statutes are found requiring executors, when selling personal property of the estate, to sell the same at public auction. When such a statute exists, a purchaser at private sale is not a *bona fide* purchaser, and is not protected, and is liable for the stocks and dividends paid thereon after his purchase.⁶ The *bona fide* transferee of such a purchaser, however, is protected.⁷ An executor may have the duties of a trustee to perform, and then become subject to the rules governing trustees in their transfers of stock.⁸

¹ *Middlebrook v. Merchants Bank*, 3 Keyes (N. Y.), 135 (1866); *Luce v. Manchester, &c., R. R. Co.*, 2 New Eng. Rep. 263 (N. H., 1886).

² *Alfonso's Appeal*, 70 Penn. St. 347 (1872), holding that, in Pennsylvania, executors of a decedent, whose domicile was in Cuba, have no authority under letters testamentary in Cuba to transfer stock in a Pennsylvania corporation. "Domestic creditors, legatees, or next-of-kin, should not be sent abroad in quest of property to answer their claims when the decedent left property within the jurisdiction of the State that can be applied to meet their demands."

³ *Goodwin v. American National Bk.*, 48 Conn. 550 (1881).

⁴ *Keeney v. Globe Mill Co.*, 39 Conn. 145 (1872).

⁵ *Prall v. Hamil*, 28 N. J. Eq. 66 (1877). The facts in this case differed from those in *Prall v. Tilt*, *supra*, in that the transferee knew that the stock was still owned by the executrix. *White v. Price*, 39 Hun, 394 (1886), the court saying: "A person who takes title from an executor, in pay-

ment of the executor's personal debts, is not a purchaser in good faith, and acquires no rights over the prior title or rights of other persons." Also, that a purchaser, buying with knowledge that the right of the executor to sell is denied and is being contested, is not a *bona fide* holder. *Cf. Keane v. Roberts*, 4 Madd. Ch. 332 (1819), where it was held that where the executor did business through an agent, the application of the proceeds from sale of the stock to the running account between the executor and his agent was legal.

⁶ *Nutting v. Thompson*, 57 Ga. 418 (1876), the court saying also that factors or brokers, acting for third persons, are also liable. *Nutting v. Boardman*, 43 Ga. 598 (1871), holding that the administrator's bondsmen are not proper parties to the suit. *Weyer v. Second Natl. Bank of Franklin*, 57 Ind. 198 (1877), holding the purchaser liable.

⁷ *Nutting v. Thomason*, 46 Ga. 34 (1872).

⁸ *White v. Price*, 39 Hun, 394 (1886); *Prall v. Tilt*, *supra*.

§ 330. *Duty and liability of the corporation.*—There has been great difficulty in ascertaining the rights and duties of the corporation in allowing and refusing to allow a registry on the corporate transfer book of a sale of stock by an executor or administrator. The Bank of England, at an early day, assumed the power to refuse to allow a registry of an executor's transfer of stock, that had been specifically bequeathed, unless the executor satisfied the bank that the sale was necessary to pay the debts of the estate. The courts, however, compelled it to allow registry without investigating specific legacies or the application of the proceeds of the sale.¹ In this country the question of the liability of the corporation has arisen on a different state of facts. The cases of *Lowry v. Commercial & Farmers Bank of Baltimore*,² and *Stewart v. Firemen's Ins. Co.*,³ clearly establish the rule that where the corporation has reasonable notice of the fact that the executor is committing a breach of trust, in that a transfer of stock by him is made several years after the estate should have been wound up, it is under obligation to refuse to allow a registry of his transfer, and, having allowed it, the corporation is liable to the parties injured thereby. Where, however, the executrix has power given by the will to apply the stock to her own use in case of need, the corporation is not bound to ascertain whether such a state of need exists.⁴

In Indiana it is held that where, by statute, executors' sales are to be at public auction, the corporation is bound to ascertain whether the statute was complied with, and to be liable for allowing a registry when the sale was a private one.⁵ In general, a corporation has a right to assume that the executor is transfer-

¹ *Pearson v. Bk. of Eng.*, 2 Brown's Ch. Rep. 529 (1789); *Bk. of Eng. v. Moffat*, 3 Id. 260 (1791); *Hartga v. Bk. of Eng.*, 3 Ves. 55 (1796); *Bk. of Eng. v. Parsons*, 5 Ves. 665 (1800); *Bk. of Eng. v. Lunn*, 15 Ves. 568 (1809); *Austin v. Bk. of Eng.*, 8 Ves. 522 (1803); *Marryatt v. Id.*, Id. 524, n. (1793); *Aynsworth v. Id.*, Id.; *Franklin v. Id.*, 1 Russ. Ch. 575 (1826); *Churchill v. Id.*, 11 M. & W. 323 (1843); *Humberstone v. Chase*, 2 Y. & C. Ex. Rep. 209 (1836), where the executor represented that the specific legatee had died.

² *Taney (U. S. C. Ct.)*, 310 (1848). The court said the corporation "not only enabled the executor to perpetrate the

wrong by permitting the transfer, but co-operated in it by certifying that the title of transferee was good. Justice, therefore, requires that it should bear the loss."

³ 53 Md. 564 (1880), holding also that the corporation was bound to take notice of the contents of the will, a position that is denied by the case of *Hutchins' Admr. v. State Bank*, 53 Mass. 421 (1847).

⁴ *Hutchins' Admr. v. State Bank*, *supra*.

⁵ *Weyer v. Second Natl. Bk. of Franklin*, 67 Ind. 198 (1877). A contrary view seems to be held in *Southwestern R. R. Co. v. Thomason*, 40 Ga. Rep. 408 (1869).

ring the stock for the purposes of the estate. It is not obliged to inquire into the purposes of the parties, nor to investigate whether the transaction is in good faith or is fraudulent.¹

¹ Crocker v. Old Colony R. R. Co., Manufacturers Natl. Bk., 71 Me. 448; Good-
137 Mass. 417 (1884). See also Carter v. win v., American Natl. Bk., 48 Conn. 550.

CHAPTER XX.

SALES OF STOCK.—FORMATION, LEGALITY, ENFORCEABILITY, AND PERFORMANCE OF A CONTRACT TO SELL STOCK.

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- 357. Fraud in selling stock may amount to a conspiracy.

A.—FORMATION AND PERFORMANCE OF CONTRACTS TO SELL STOCK.

§ 331. *Shares of stock are transferable.*—That shares of stock in a corporation are transferable the same as other personal property is a principle of law, coeval with the existence of stock itself. The few decisions, holding that shares of stock were real estate, were exceptional rulings, and are no longer considered to be good law.¹ Courts of law and of equity have guarded jealously the facilities for the transfer of title to stock, and all unreasonable attempts to restrain the right or readiness

¹ See Ch. I.

of passing title, have been declared void as against public policy. The right to transfer stock is of vital importance, since the two chief causes of the phenomenal growth of corporations in recent times, are the limited liability of the members, and the readiness of withdrawing from the corporation by a transfer of the interest a member has therein.¹ The common law regards shares of stock as personal property, capable of alienation or succession in any of the modes by which personal property may be transferred.²

§ 332. *Restrictions on right to sell stock.*—The right of a stockholder to sell and transfer his stock, cannot be restrained by a by-law of the corporation.³ An agreement or contract, however, between the members or a part of them, not to sell except on certain conditions, is valid, unless it amounts to an unreasonable restraint of trade.⁴ The right of transfer is sometimes limited by statute, as in New York, where stock in railroad or manufacturing corporations cannot be transferred until all calls thereon shall have been fully paid.⁵ Where the charter or a statute forbids transfers before the full capital stock is paid in, any transfer before such payment has been held to be void.⁶

¹ See § 339. "Many persons enter these companies for the very reason that they are not like ordinary partnerships, but they are partnerships from which members can retire at once, and free themselves from responsibility at any time they please, by going into the market and disposing of and transferring their shares without the consent of directors or shareholders, or anybody, provided only it is a *bona fide* transaction." *Weston's Case*, L. R., 4 Ch. 20, 27 (1868). "It is one of the leading objects of an incorporated body to avoid the operation and effect of this doctrine of the law of partnership. Accordingly, in this country, shares in corporations are universally bought and sold without reference to the consent of the other shareholders." "The restrictions on the right, *bona fide*, to sell and transfer shares, must be found in express legislative enactments, or in authorized by-laws." *Dillon, J., in Johnson v. Laffin*, 5 Dill. 63 (1878).

² *Mobile Mutual Ins. Co. v. Cullum*, 49 Ala. 558 (1873); *Cole v. Ryan*, 52 Barb. 168 (1868); *Heart v. State Bk.* 2 Dev. Eq. 111 (1831); *Allen v. Montgomery R.*

R. Co., 11 Ala. 437, 451 (1847); *Boston Music Hall v. Cory*, 129 Mass. 435 (1880); *Sargent v. Franklin Ins. Co.*, 8 Pick. 90 (1829); *Chouteau Spring Co. v. Harris*, 20 Mo. 382 (1855); *Poole v. Middleton*, 29 Beav. 646 (1861); *Brightwell v. Mal-lory*, 10 Yerg. (Tenn.) 196 (1836).

³ *Fechheimer v. Natl. Ex. Bk.* (Va. May, 1884); *Bank of Attica v. Manufacturers and T. Bk.*, 20 N. Y. 501 (1859); *Orr v. Bigelow*, 14 N. Y. 556 (1856); *Sargent v. Franklin Ins. Co.*, 8 Pick. 90 (1829); *Moore v. Bk. of Com.*, 52 Mo. 377 (1873), the court saying: "The right of alienation is an incident of property, and a by-law prohibiting this right, or imposing any restrictions on its exercise, would be in restraint of trade and against public policy." See also *Ch. on Liens*.

⁴ *Griffith v. Jewett*, 15 Week. L. Bul. 419. See § 340, note 5.

⁵ N. Y. Session Laws, 1850, ch. 140, § 8; 1848, ch. 40, § 8.

⁶ *Merrill v. Call*, 15 Me. 428. The case of *Quiner v. Marblehead Ins. Co.*, 10 Mass. 476 (1813), holds that nevertheless such a transfer vests in the transferee all the transferor's interest in the stock.

In England, sometimes, express authority is given to the directors, by the articles of association, to refuse to permit a transfer, unless the same is satisfactory to them.¹ They have this power, however, only by this express authority, and it is not extended by implication.² The power must be reasonably exercised, and its exercise must be free from fraud, caprice, and arbitrary power.³ But the board may refuse to give its reasons for refusing to allow the transfer, and in that case it will be presumed to have had sufficient reason for the refusal.⁴ Although a transfer is rejected by the directors the transferee is nevertheless entitled to dividends, and the title to the stock.⁵ The corporation cannot refuse to allow a registry on the ground that there was no consideration for the transfer;⁶ nor because a claimant of the stock notifies it not to make the registry.⁷ A registry of a transfer of stock cannot be refused merely because the old stockholder is indebted to the corporation. This would give the corporation a lien on the stock of its shareholders, and such a lien cannot exist even by way of a by-law, although of course it may be granted by the charter itself.⁸ A by-law, however, it has been held, may be made, prohibiting a registry of transfer, until the old stockholder has liquidated his indebtedness to the other stockholders.⁹ Such a by-law, however, can have effect only as a contract of which the stockholder is to be given notice upon his becoming such.

¹ *Shortridge v. Bosanquet*, 16 Beav. 84 (1852); *Bargate v. Shortridge*, 5 H. L. Cases, 297 (1855).

² *Weston's Case*, L. R., 4 Ch. App. 20 (1868); *Gilbert's Case*, L. R., 5 Ch. App. 559 (1870); *Chappell's Case*, L. R., 6 Ch. App. 902 (1871). *Re Stranton Iron & Steel Co.*, L. R., 16 Eq. 559 (1873). Judge Dillon, in *Johnson v. Laffin*, 5 Dill. 65, 78; aff'd 103 U. S. 800, says: "Such a power is so capable of abuse and so foreign to all received notions, and the universal practice and mode of dealing in these stocks, that it cannot, in the absence of legislative expression, be held to exist." See also *Farmers & M. Bk. v. Wasson*, 48 Iowa, 336 (1878), the court holding that a by-law that transfers of stock shall not be valid unless approved by the board of directors cannot restrain transfers. "Its enforcement would operate as an infringement upon the property rights of others, which the law will not permit. It would,

besides, operate as a restraint upon the disposition of property in the stock of the corporation, in the nature of restraint of trade, which the courts will not tolerate."

³ They cannot refuse to allow any transfers. *Robinson v. Chartered Bank*, L. R., 1 Eq. 32 (1865), and an objection, not to the transferee, but to the purpose of the transferrer, in respect to voting, is not sufficient. *Moffatt v. Farquhar*, L. R., 7 Ch. D. 591 (1878).

⁴ *Ex parte Penny*, L. R., 8 Ch. 446 (1872).

⁵ *Poole v. Middleton*, 29 Beav. 646 (1861).

⁶ *Helm v. Swiggett*, 12 Ind. 194 (1859).

⁷ *Ex parte Sargent*, L. R., 17 Eq. 273 (1873).

⁸ See Ch. XXII.

⁹ *People v. Miller*, N. Y. Supr. Ct., Daily Reg., April 10th, 1886, a case arising in the Cotton Exchange of New York.

§ 333. *Contract for sale of stock may be valid without delivery or specific time for delivery.*—Generally a sale of stock is attended with an immediate delivery of the certificates therefor, or it is agreed that the certificates shall be delivered at some specified time in the future. If, however, the vendor offers to sell his stock and the vendee accepts the offer, the contract is complete and binds both parties, although nothing has been said as to the time when the certificates of stock shall be delivered. The law implies that the contract will be performed by a delivery of the certificates immediately or within a reasonable time, and either party may insist upon carrying out the contract.¹ Where the vendor says, in his contract, "I have sold" certain stock, deliverable at seller's option, within a specified time, a sale *in presenti* is made and the vendor assumes to have the stock and to hold it for the benefit of the purchaser until delivery.² An agreement to purchase stock when the corporation is created, is enforceable only after a complete and legal incorporation is effected.³ A sale of stock with an agreement to take it back whenever the vendee desires, is an enforceable contract.⁴

§ 334. *Method of performance or offer of performance by vendor.*—A person who is under contract to sell and deliver

¹ "The performance of a contract, or the tender of performance, is no part of the contract. The making of a contract is one thing, but the performance thereof, or the tender of performance, is another and quite different thing. The contract set up in the paragraph in question is an executory one, by which the plaintiff agreed to sell to the defendant the shares of the stock, and the defendant agreed to pay him therefor the sum of \$2,500. No time was fixed for the performance; the law will imply therefore that it was to be performed immediately, or perhaps within a reasonable time. Had a future day been agreed upon for the performance of the contract on each side, there could have been no doubt as to its validity, or the right of either party to enforce it, he having done all he was required to do on his part. The fact that no time was agreed upon for performance does not change the character of the contract. The contract did not pass any title to the stock, but it was, nevertheless, a valid contract, and one which either party can enforce, he hav-

ing been in no default himself." *Bruce v. Smith*, 44 Ind. 1 (1873); *Kerchuer v. Gettys*, 18 S. C. 521 (1882); *Cheale v. Kenward*, 3 De G. & J. 27 (1858). An agreement of the vendor of railroad bonds, to take back the bonds whenever the vendee desired him to do so, is a valid and enforceable contract. *Fitzpatrick v. Woodruff*, 96 N. Y. 561 (1884). *Cf. Meyer v. Blair*, N. Y. Daily Reg. Nov. 11, 1886. Usage may determine what is a reasonable time for delivery. Seven days held reasonable. *Stewart v. Cauty*, 8 M. & W. 160 (1841). *Cf. § 339.*

² *Currie v. White*, 45 N. Y. 822 (1871). When the option is exercised the time of delivery as fixed is as though that time had been specified in the original contract. *Kelley v. Upton*, 5 Duer, 336 (1866), holds otherwise where the contract has also the words "at buyer's option in 90 days." Such a contract is executory as to time of passing title, and tender is necessary.

³ *Childs v. Smith*, 55 Barb. 45 (1869).

⁴ See § 339.

shares of stock, may fulfill the obligation on his part by tendering to the vendee certificates of stock duly indorsed by himself, and containing a power of attorney authorizing the vendee to obtain a registry of the transfer on the corporate books.¹ It has been held, however, and evidently with good reason, that if the vendee objects to the tender, on the ground that he wishes a registry of the transfer to be made on the corporate books, the vendor must cause such registry to be made, in order to render his tender complete.² A tender of certificate indorsed in blank, not by the vendor, but by some previous owner, is insufficient. The vendee is not obliged to trace his vendor's title from the name appearing on the certificate.³ In England, where a transfer of shares is to be made by a deed, it is the duty sometimes of the vendor,⁴ and sometimes of the vendee,⁵ to furnish the necessary deed, according to the custom of the market in which the sale is made. If, after the vendee accepts a tender of the certificates, the corporation refuses to allow a registry and transfer on the corporate books, the vendor is liable to him, since the registry is held to have been guaranteed.⁶ The vendee may decline to accept the certificates if the stock has been attached.⁷ But the vendee cannot decline the tender on the ground that the corporation has issued stock at a discount, nor because it has mortgaged its property.⁸ A contract whereby stock is sold to be paid for in the future, is not forfeited by mere failure to pay as agreed upon.⁹

§ 335. *Remedy by action for damages for breach of contract to buy or sell stock.*—The ordinary and clearest remedy by one party to a contract for the sale of stock against the other party to

¹ "When certificates of shares are given to a purchaser, they are analogous to the sale of chattels, and the "assignment and delivering of the certificate is a symbolical delivery of the shares themselves." *Noyes v. Spaulding*, 27 Vt. 420 (1855); *Merchants Nat'l Bk. v. Richards*, 6 Mo. App. 454 (1879); *Eastman v. Fiske*, 9 N. H. 182 (1838); *Munn v. Barnum*, 24 Barb. 283 (1857); *Bruce v. Smith*, 44 Ind. 1 (1873). *Cf.* *Moore v. Hudson River R. R. Co.*, 12 Barb. 156.

² *White, Executor v. Salisbury*, 33 Mo. 150 (1862).

³ *Hare v. Waring*, 3 M. & W. 362 (1838), per B. Parke: "The party is to convey and deliver certificates showing either on the face of them or from the in-

dorsements that the title is in the person conveying."

⁴ *Stephens v. De Medina*, 4 Q. B. 422 (1848).

⁵ *Shaw v. Rowley*, 16 M. & W. 810 (1847).

⁶ *Wilkinson v. Lloyd*, 7 Q. B. 27 (1845).

⁷ *Eastman v. Fiske*, 9 N. H. 182 (1838).

⁸ *Noyes v. Spaulding*, 27 Vt. 420 (1855).

⁹ *Chater v. San Francisco Sugar Refining Co.*, 19 Cal. 219 (1861), where payment was made in notes and labor, and the notes were not paid. Subsequent dividends on the stock are to be applied to the payment of such notes, when the dividends have been received by the vendor.

that contract for refusal to fulfill, is an action at law for damages. This remedy is available to either the party who contracted to sell, or the party who contracted to buy. If the damage done to the complaining party is clearly ascertainable in money, this remedy is an exclusive one. The measure of damages to which the aggrieved party is entitled has been the occasion of great difference of opinion and is treated of elsewhere.

§ 336. *Miscellaneous defenses to an action for damages for failure to complete a contract for the sale of stock.*—A person who is under contract to purchase stock cannot defeat that contract by the fact that the corporation was insolvent, even at the time the contract was entered into.¹ An agreement to deliver stock free and clear of all incumbrances, does not refer to incumbrances against the corporation.² The legality of the sale of stock is governed by the law of the State within which it is made.³ It is no defense to a contract to buy stock for the vendee to allege that the directors have committed an *ultra vires* act in issuing more stock at a discount.⁴

§ 337. *Specific performance as a remedy for breach of a contract to sell stock.*—It frequently happens that the person who has contracted to purchase stock is particularly anxious to procure that stock, and that under the circumstances of the case, the stock is worth to him a value not to be compensated for by mere money damages. This cannot happen in the case of a contract to sell securities issued by the government, since they may be duplicated and easily purchased in the market. Accordingly, it is well established, both in England and America, that a contract for the sale of government securities, will not be specifically

¹ Rudge v. Bowman, L. R. 3 Q. B. 689 (1868); Gordon v. Parker, 10 La. Rep. 56 (1836), where the question of whether fraud was involved was submitted to the jury. Crubb v. Miller, 19 W. R. 519 (1871), where by reason of a winding up a transfer on the corporate books is no longer possible. Kerchuir v. Gettys, 18 S. C. 521 (1882), holding that a loss by the corporation of its property is no defense.

² Williams v. Hanna, 40 Ind. 535 (1872).

³ Dow v. Gould & C. S. M. Co., 31 Cal. 629 (1867).

⁴ "If this was a legal act it was one which the defendant was bound to know the directors might do, and which would therefore form one of the contingences of his purchase, and which, whether done before or after the actual time of sale, could no more affect the validity of the sale than any other legal act of the directors. If the act was an unlawful exercise of authority, the defendant, when he became a stockholder, might resist it in any legal way." Faulkner v. Hebard, 26 Vt. 452 (1854). That fraud is a defense, see §§ 349-357.

enforced by a court of equity, but the vendee may sue the vendor in an action at law for damages for breach of contract.¹

§ 338. An entirely different rule prevails as regards contracts for the sale of stock of private corporations. If the stock contracted to be sold is easily obtained in the market, and there are no particular reasons why the vendee should have the particular stock contracted for, he is left to his action for damages. But, where the value of the stock is not easily ascertainable, or the stock is not to be obtained readily elsewhere, or there is some particular and reasonable cause for the vendee's requiring the stock contracted to be delivered, a court of equity will decree a specific performance and compel the vendor to deliver the stock. This rule, as applicable to contracts for the sale of railway stock, was clearly enounced in England, in 1841, in the case *Duncuft v. Albrecht*.² Contracts for the sale of stock in mining and other private corporations, will also be specifically enforced under like circumstances.³ Specific performance will not be

¹ *Ross v. Union Pacific Ry. Co.*, 1 Woolw. 26, 32 (1863); *Cud or Cuddee v. Rutter*, 1 P. Wms. Rep. 570; 5 *Viner's Abr.* 538 (1715); *Dorison v. Westbrook*, 5 *Viner's Abr.* 540 (1722); *Cappur v. Harris*, *Bunbury's Rep.* 135 (1723); *Colt v. Netterville*, 2 P. Wms. 304 (1725); *Buxton v. Lister*, 3 Atk. 383 (1746). *Cf.* *Daloret v. Rothschild*, 1 Sim. & S. 590 (1824).

² "It has been long since decided that you cannot have a bill for the specific performance of an agreement to transfer a certain quantity of stock. But, in my opinion, there is not any sort of analogy between a quantity of 3 per cents. or any other stock of that description, (which is always to be had by any person who chooses to apply for it in the market,) and a certain number of railway shares of a particular description, which railway shares are limited in number, and which, as has been observed, are not always to be had in the market. And as no decision has been produced to the contrary, my opinion is that they are a subject with respect to which an agreement may be had which this court will enforce." *Duncuft v. Albrecht*, 12 Sim. 189 (1841); *Parish v. Parish*, 32 Beav. 207 (1863), granting also an accounting of dividends; *Poole v. Middleton*, 29 Beav. 646 (1861); *Turner v. May*, 32 L. T. N. S. 56 (1875); *Beckett v. Billsbrough*, 8

Hare, 188 (1850), *dictum*. *Contra, dictum* in *Ross v. Union Pacific Ry. Co.*, 1 Woolw. 26, 32 (1863), per Miller, J. In *Cheale v. Kenward*, 3 De G. & J. 27 (1858), the court said: "There is no doubt that a bill will lie for a specific performance of an agreement to transfer railway shares. This was set at rest by *Duncuft v. Albrecht*." In the case *Leach v. Fobes*, 77 Mass. 506 (1858), specific performance of a contract to convey land and real estate was granted, chiefly because of the land part of the contract. *Todd v. Taft*, 89 Mass. 371 (1863), decreed specific performance of a contract to convey railway shares; also *Baldwin v. Commonwealth*, 11 Bush, 417 (1875); *Ashe v. Johnson's Administrator*, 2 Jones' Eq. (N. C.) 149 (1855).

³ "In the peculiar condition of business and mining operations in this State, where numerous mining and other corporations are in existence, whose stock is often of fluctuating and uncertain value, and where certain kinds of stock have a peculiar value to those acquainted with their affairs, where the market value of stocks, if any they have, is often difficult to substantiate by competent evidence, and where the risk of personal responsibility of individuals and corporations is so great, courts should be liberal in extending the full, adequate, and complete relief afforded by a decree of specific

granted, however, where the purpose of the purchaser of stock is to obtain control of a national bank, when the change in management would probably be to the detriment of the bank.¹ Where the vendor's contract is to deliver stock and construct a railway, the court will not decree specific performance, since part of the contract is never the subject of such compulsory performance.² If the vendor is not in possession of the desired stock, specific performance will not be granted,³ except to the amount of stock which he has.⁴ Although a court of equity refuses to grant specific performances, yet it will not send the party to a court of law, but will grant him damages.⁵ Specific performance sometimes lies at the instance of the vendor of stock. It has been held that where the enterprise is not yet completed and the liability not ascertainable, equity will compel the vendee to accept the stock.

§ 339. *Seventeenth section of Statute of Frauds as affecting sales of stock.*—In England the rule is firmly established that the seventeenth section of the Statute of Frauds, relating to contracts for the sale of "goods, wares, and merchandise," does not apply to sales of stock. No delivery, payment of earnest money, or memorandum in writing is necessary, in order to render

performance." *Treasurer v. Commercial Coal Min. Co.*, 23 Cal. 390 (1863). See also *Erne v. Houghton*, 6 Col. 318 (1882). As applicable to manufacturing corporations, see *Chater v. San Francisco S. R. Co.*, 19 Cal. 200 (1861). Granted in *Tow Boat Association in White v. Schuyler*, 1 Abb. Pr. N. S. 300 (1863). Refused in the case of stock in a land association, *Jones v. Newhall*, 115 Mass. 244 (1874); and in a paper company, *Noyes v. Marsh*, 123 Mass. 286 (1877). See *Cushman v. Thayer Mfg. Co.*, 76 N. Y. 365 (1879). "While the general rule is for courts of equity not to entertain jurisdiction for a specific performance on the sale of stock, this rule is limited to cases where a compensation in damages would furnish a complete and satisfactory remedy." This case, however, is not a case of specific performance of a sale of stock, but of compelling the corporation to register a transfer. See also, in general, *Austin v. Gillaspie*, 1 Jones' Eq. 261; *Nutbrown v. Thornton*, 10 Vesey, 180; *Shaw v. Fisher*, 5 De G., M. & G. 596; *Wynne v. Price*, 3 De G. & Sm. 310;

Wilson v. Keating, 7 W. R. 484; *Oriental Co. v. Briggs*, 2 J. & H. 625; *Paine v. Hutchinson*, L. R. 3 Eq. 257; *Shepherd v. Gillespie*, L. R. 5 Eq. 293; *Birmingham v. Sheridan*, 33 Beav. 660; *Strasbourg v. Echternacht*, 21 Penn. St. 220; *Fallon v. R. R. Co.*, 1 Dill. 121. In regard to a specific performance of a trust of stock, see *Ferguson v. Paschall*, 11 Mo. 267; *Cowles v. Whitman*, 10 Conn. 121; *Clark v. Flint*, 22 Pick. 231; *Mechanics Bk. v. Seton*, 2 Peters, 299.

¹ *Foll's Appeal*, 91 Penn. St. 434 (1879), the court saying: "I know of no instance in this State in which a court of equity has decreed specific performance of a sale of stock."

² *Ross v. Union Pacific Ry. Co.*, 1 Woolw. 26 (1863), per Miller, J.

³ *Columbine v. Chichester*, 2 Phil. Ch. 27 (1846).

⁴ *Turner v. May*, 32 L. T. N. S. 56 (1875).

⁵ *Wonson v. Fenno*, 129 Mass. 405 (1880); *Austin v. Gillespie*, 1 Jones' Eq. (N. C.) 261 (1854).

the contract of sale valid. This principle of law was doubted in the early cases,¹ but was determined by the case *Humble v. Mitchell*, in 1839.² In 1838 this question arose in this country, apparently for the first time, and it was decided, in *Tisdale v. Harris*,³ chiefly on the authority of the early English cases, that a contract for the sale of stock was within the seventeenth section of the Statute of Frauds. This decision has been uniformly followed in America.⁴ A broker, however, as a common agent, may make the memorandum for both parties.⁵ A subsequent part payment of the consideration makes the contract valid,⁶ and a payment in property⁷ or services,⁸ suffices. The statute does not apply as between partners for the purpose of buying stock.⁹ A contract for the sale of stock in a corporation not yet incorporated, has been held not to be within the statute.¹⁰ The statute must

¹ *Mussell v. Cooke*, Finch Prec. in Ch. 533 (1720), holding that the statute applied but was not properly pleaded; *Pickering v. Appleby*, 1 Comyns Rep. 353 (1721), not decided, the judges being divided, six and six. *Colt v. Netterville*, 2 P. Wms. 306 (1725), not decided, the Lord Chancellor saying it was too difficult to decide on a demurrer. *Crull v. Dodson*, Sel. Ca. in Ch. Temp. King (fol. 41, 1724), statute held to apply.

² 11 A. & E. 205, followed in *Duncuft v. Albrecht*, 12 Sim. 189 (1841), the court saying that the statute applies only to goods capable of part delivery. *Hibblewhite v. McMorine*, 6 M. & W. 201, 214 (1840); *Tempest v. Kilner*, 3 C. B. 249 (1846); *Heseltine v. Siggers*, 1 Ex. 856 (1848).

³ 27 Mass. (20 Pick.) 9.

⁴ *Baltzen v. Nicolay*, 53 N. Y. 467 (1873), rigidly applying the rule; *North v. Forrest*, 15 Conn. 400 (1843), where the court says: "Such contracts fall clearly within the mischiefs which the legislature, by the statute, intended to remedy. There is as much danger of fraud and perjury, in the parol proof of such contracts, as in any other." *Pray v. Mitchell*, 60 Me. 430 (1872); *Fine v. Hornaby*, 2 Mo. App. 61 (1876); *Colvin v. Williams*, 3 Har. & Johns. (Md.) 38 (1810); *Sherwood v. Tradesman's Nat'l Bank*, 16 N. Y. W. Dig. 522 (1883, Supreme Ct.). Cf. *Brownson v. Chapman*, 63 N. Y. 625. *Contra, dictum, Vawter v. Griffin*, 40 Ind. 593, 602 (1872). See Reed on Statute of Frauds, § 234; *Hagar v. King*, 38 Barb. 200 (1862), holding that the sale of rail-

road bonds is within the statute. In Florida the statute applies, the word personal property being used. *Southern Life Ins. Co. v. Cole*, 4 Fla. 359, 378. See also *Mason v. Decker*, 72 N. Y. 595; aff'g 10 J. & S. 115; *Johnson v. Mulry*, 4 Rob. (N. Y.) 401 (1867), holding that the New York Stock Jobbing Act (Laws N. Y. 1858, ch. 184) did not affect the application of the Statute of Frauds. The statute is not sufficiently pleaded by alleging that the contract of sale of stock "was void in law and not binding upon him." *Vaupell v. Woodward*, 2 Sand. Ch. 143.

⁵ *Calvin v. Williams*, 3 Hare & J. 38 (1810).

⁶ *Thompson v. Alger*, 53 Mass. (12 Metc.) 428 (1847).

⁷ *Eastern R. R. Co. v. Benedict*, 76 Mass. (10 Gray), 212 (1857).

⁸ *White v. Drew*, 56 How. Pr. 53 (1878), holding that the furnishing of reliable information is sufficient.

⁹ *Tomlinson v. Miller*, 7 Abb. Pr. N. S. 364 (1869). Nor as between persons, one of whom buys stock in his own name for the joint benefit of both. *Storer v. Flack*, 41 Barb. 162 (1862).

¹⁰ *Gadsden v. Lance*, 1 McMull Eq. (S. C.) 87 (1841); *Green v. Brookins*, 23 Mich. 48, 54 (1871), where a person was induced to subscribe on parol contract that a purchaser for the stock would afterwards be found. In Massachusetts, on similar facts, except that a certain person agreed to purchase, a contrary decision was rendered. *Boardman v. Cutter*, 128 Mass. 388 (1880).

be pleaded in order to be effectual as a defense.¹ The assignee of a contract for the sale of stock, void by the Statute of Frauds, takes nothing by the assignment.² An agreement by the vendor of stock to take it back at any time, is not affected by the statute, and such an agreement is a part of the executed sale.³

§ 340. *Other sections of Statute of Frauds as affecting sales of stock.*—The provision of the Statute of Frauds relative to answering for the debts, defaults, or miscarriages of another, does not apply to a guarantee that there will be a certain dividend on stock purchased,⁴ nor to a broker's relation towards his client.⁵ The provision of the statute relative to transfers of land do not apply to stock,⁶ since shares of stock are personal property.⁷ A transfer of stock for the purpose of defrauding the transferrer's creditors is void, and a court of equity will set it aside,⁸ or the stock may be attached or sold under execution the same as though no attempt at transfer had been made.⁹

B.—GAMBLING SALES OF STOCK.

§ 341. *What are wager stock sales.*—Executory contracts for the sale of stock may be made with an intent to actually deliver the stock, or may be with an intent not to deliver it, but to pay, in cash the amount lost or won by the rise or fall of the market price of the stock. A sale with the former intent is, at common law, legal and valid.¹⁰ A sale with the latter intent is a gambling or

¹ *Porter v. Wormser*, 94 N. Y. 431, 450 (1884).

² *Mayer v. Child*, 47 Cal. 142 (1873).

³ *Fitzpatrick v. Woodruff*, 96 N. Y. 561 (1884); *Thorndike v. Locke*, 98 Mass. 340 (1867); *Fay v. Wheeler*, 44 Vt. 292 (1872). See also § 333.

⁴ *Moorehouse v. Crangle*, 36 O. St. 130 (1880).

⁵ *Genin v. Isaacsen*, 6 N. Y. Leg. Obs. 213; *Rogers v. Gould*, 6 Hun. 229 (1875).

⁶ *Watson v. Spratley*, 10 Ex. 222; *Powell v. Jessopp*, 18 C. B. 335 (1856); *Walker v. Bartlett*, 18 C. B. 845 (1856); *Ashworth v. Munn*, 14 Ch. D. 363, 368 (1880).

⁷ See Chapter I.

⁸ *Skowhegan Bank v. Cutter*, 49 Me. 315 (1860); *State v. Warren F. & M. Co.*, 32 N. J. Law Rep. 439 (1868); *Bayard v. Hoffman*, 4 Johns. Ch. 450 (1820); *Had-den v. Spader*, 20 Johns. Rep. 554 (1822);

Scott v. Indianapolis Wagon Works, 48 Ind. 75 (1874); *Moore v. Metropolitan Natl. Bk.*, 55 N. Y. 41 (1873). The fraudulent transferee must be made a party defendant. *Hyatt v. Swivel*, 52 N. Y. Super. Ct. 1 (1885). See also Ch. XXVII. But the fraudulent transferee is not liable unless he has accepted the stock. *Skowhegan Bank v. Cutler*, 49 Me. 315 (1860); *Cartwell's Case*, L. R. 9 Ch. 691 (1874). Acceptance is a question of fact. *Pim's Case*, 3 De G. & S. 11 (1849). But he cannot plead the Statute of Frauds himself. *Smith v. 49 & 56 Quartz M. Co.*, 14 Cal. 242 (1859).

⁹ *Beckwith v. Burroughs*, R. I., Feby. 9, 1884. See Ch. XXVII.

¹⁰ *Irwin v. Williar*, 110 U. S. 499, 508 (1883). "The generally accepted doctrine in this country is . . . that a contract for the sale of goods to be delivered at a future day is valid, even though the

wager contract, and is not enforceable.¹ The essential difference between a wager contract and a contract not a wager is whether there is an intent to deliver the property sold.²

seller has not the goods nor any other means of getting them than to go into the market and buy them; but such a contract is only valid when the parties really intend and agree that the goods are to be delivered by the seller and the price to be paid by the buyer; and if under guise of such contract the real intent be merely to speculate in the rise or fall of prices, and the goods are not to be delivered, but one party is to pay to the other the difference between the contract price and the market price of the goods at the date fixed for executing the contract, then the whole transaction constitutes nothing more than a wager, and is null and void. And this is now the law in England by force of the statute of 8 & 9 Vict. c. 109, s. 18, altering the common law in that respect."

It may be speculation, nevertheless it is valid. *Clark v. Foss*, 7 Biss. 540 (1878), where the court says, in reference to sales of property which the vendor intends to buy hereafter for the purpose of delivery: "Such contracts, although entered into for pure purposes of speculation, however censurable, when made by those engaged in ordinary mercantile pursuits, and who have creditors depending for the payment of their just claims upon their prudent management in business, are, nevertheless, not prohibited by law." To same effect, *Smith v. Bouvier*, 70 Penn. St. 325; *Kirkpatrick v. Bonsall*, 72 Penn. St. 155 (1872), where the court says: "We must not confound gambling, whether it be in corporation stocks or merchandise, with what is commonly termed speculation. Merchants speculate upon the future prices of that in which they deal, and buy and sell accordingly." *Hatch v. Douglas*, 48 Conn. 116 (1880); *Flagg v. Baldwin*, 38 N. J. Eq. Rep. 219; *Kent v. Miltenberger*, 13 Mo. App. 503 (1883).

¹ "Wagers at common law are valid and enforceable in the courts;" and, with certain exceptions growing out of the peculiar subject of the wager, are valid contracts. Dewey on Contracts for Future Delivery, and Commercial Wagers (1886), 10. To same effect, *Good v. Elliott*, 3 Term R. 693 (1790); *Gilbert v. Sykes*, 10 East, 150; *Atherford v. Beard*, 2 Term R. 610 (1788); *Morgan v. Pebrer*, 4 Sco. 230 (1837); *Hussey v. Crickitt*, 3 Camp. 693;

Grant v. Hamilton, 3 McLean, 100 (1842); *Campbell v. Richardson*, 10 Johns. 406 (1813); *Bunn v. Riker*, 4 Johns. 436 (1809); *Johnson v. Fall*, 6 Cal. 359 (1856); *Johnston v. Russel*, 37 Cal. 670 (1869); *Deweese v. Miller*, 5 How. 347 (1848); *Porter v. Sawyer*, 1 How. 519 (1832); *Griffith v. Pearce*, 4 Houston, 209 (1869); *Richardson v. Kelley*, 85 Ill. 491 (1877); *Pettit v. Hipple*, 90 Ill. 420 (1878); *Trenton Ins. Co. v. Johnson*, 2 Zab. 526; *Dunman v. Strother*, 1 Texas, 89 (1846); *McElroy v. Carmichael*, 6 Texas, 464 (1851); *Wheeler v. Friend*, 22 Texas, 683 (1859); *Monroe v. Smeiley*, 25 Texas, 486 (1860). *Contra*—in Pennsylvania—*Edgell v. McLoughlin*, 6 Whar. 176 (1841); *Phillips v. Ives*, 1 Rawle, 36 (1828); *Bruas' Appeal*, 55 Penn. St. 294 (1867); in Vermont—*Collamer v. Day*, 2 Vt. 144 (1829); *Tarlton v. Baker*, 18 Vt. 9 (1843); New Hampshire—*Clark v. Gibson*, 12 N. H. 386 (1841); *Winchester v. Metter*, 52 N. H. 507 (1872); in Maine—*McDonough v. Webster*, 68 Me. 530 (1878); *Gilmore v. Woodcock*, 69 Me. 118 (1879); Missouri—*Waterman v. Buckland*, 1 Mo. App. 45 (1876); and Massachusetts—*Ball v. Gilbert*, 12 Met. 399 (1847); *Babcock v. Thompson*, 3 Pick. 446 (1826); *Sampson v. Shaw*, 101 Mass. 150 (1869). The Supreme Court of the United States says, in *Irwin v. Williar*, *supra*: "In England, it is held that the contracts, although wagers, were not void at common law, . . . while generally, in this country, all wagering contracts are held to be illegal and void as against public policy," citing *Dickson's Executor v. Thomas*, 97 Penn. St. 278 (1881); *Gregory v. Wendell*, 40 Mich. 432 (1879); *Lyon v. Culbertson*, 83 Ill. 33 (1876); *Melchert v. American U. Tel. Co.*, 3 McCrary, 521 (1882); 11 Fed. Rep. 193; *Barnard v. Bockhaus*, 62 Wis. 593 (1881); *Love v. Harvey*, 114 Mass. 80 (1873).

² *Roundtree v. Smith*, 108 U. S. 269 (1882); *In re Hunt*, 26 Fed. Rep. 739 (1886). Dewey, in his recent work on Contracts for Future Delivery, and Commercial Wagers, states the rule accurately as follows: "Where the parties to a contract in the form of a sale agree expressly or by implication at the time it is made that the contract is not to be enforced, that no delivery is to be made, but the

§ 342. *Statutes prohibiting wager contracts, and also certain stock contracts.*—There are two classes of statutes affecting stock sales as regards their speculative character. One class do not specify sales of stock, but declare in general terms that all gaming and wagering contracts shall be void, thereby rendering actions for the recovery of money won on such wagers unsustainable. Such statutes exist in England¹ and New York.² The second class of statutes are more explicit, and prohibit specified transactions in stock, irrespective of whether such transactions be wager contracts or not. Statutes affecting speculative sales of stock exist in many of the States: in Massachusetts short sales are prohibited;³ in Pennsylvania, sales for future delivery;⁴ in Ohio, sales of stock for future delivery, where the vendor has it not on hand, or the vendee the means to pay;⁵ in Illinois, all options are made gambling contracts, and are void;⁶ in Georgia, short sales cannot be enforced;⁷ in New York, the statute of 1812,⁸ re-enacted in the Revised Statutes of 1828,⁹ prohibiting

contract is to be settled by the payment of the difference between the contract price and the market price at a given time in the future, such a transaction is a wager," citing many cases.

¹ 8 & 9 Vict., c. 109, § 18; Grizewood v. Blane, 11 C. B. 526 (1851). Agreements between buyers and sellers of stock to pay or receive the differences between their prices on one day, and their prices on another day, are gaming and wagering transactions within the meaning of the statute. Thacker v. Hardy, L. R. 4 Q. B. D. 687 (1878). The statute does not necessarily affect "corners" in stocks. Barry v. Croskey, 2 J. & H. 1 (1861). As to the application of this statute, see also Heinman v. Hardie, 12 Ct. of Ses. 406 (Sc., 4th series, 1885).

² 1 R. S. of N. Y. 662, § 8 (vol. III, p. 1962, 7th ed.). As applied to stock cases, see Kingsbury v. Kirwan, 77 N. Y. 612 (1879); Story v. Saloman, 71 N. Y. 420 (1877); Harris v. Tumbidge, 83 N. Y. 92 (1880); Yerkes v. Saloman, 11 Hun, 471 (1877).

³ Gen. Stat. Mass. ch. 105, § 6. For cases arising under this statute, see Howe v. Starkweather, 17 Mass. 243 (1821); Sargent v. Franklin Ins. Co., 25 Mass. 98 (1829); Barrett v. Mead, 92 Mass. 337 (1865); Brigham v. Mead, 92 Mass. 245 (1865); Barrett v. Hyde, 73 Mass. 160 (1855); Durant v. Burt, 98 Mass. 161

(1867); Brown v. Phelps, 103 Mass. 313 (1869); Price v. Minot, 107 Mass. 49 (1871); Colt v. Clapp, 127 Mass. 476 (1879); Rock v. Nicholls, 85 Mass. 342 (1862); United States v. Vaughan, 3 Binn. 394 (1811); Wyman v. Fiske, 85 Mass. 238 (1861); Pratt v. American Bell Tel. Co., 5 Northeastern Rep. 307 (1886), following the decisions under the New York statute from which the statute in question was copied.

⁴ Laws of Penn., 1841, p. 398, § 6. This statute has been repealed. For decisions, see Krause v. Setley, 2 Phil. Rep. 32 (1856); Chillas v. Snyder, 1 Id. 289 (1850).

⁵ Ohio Laws, May, 1885.

⁶ Revised Stat. of Ill., § 178. For decisions, see Wolcot v. Heath, 78 Ill. 433 (1875); Pickering v. Cease, 79 Ill. 328 (1875); Pixley v. Boynton, 79 Ill. 351 (1875); Sanborn v. Benedict, 79 Ill. 309; Cole v. Milmine, 88 Ill. 349 (1878). This statute is restricted by the decisions to cases where the transaction is to be "adjusted only by differences."

⁷ Georgia Code, § 2638.

⁸ 2 R. L. 187, § 18.

⁹ 1 R. S., p. 710, § 6. For cases coming under this statute, see Dykers v. Townsend, 24 N. Y. 57 (1861), disapproving Stebbins v. Leowolf, 3 Cush. 143 (1849). See also Thompson v. Alger, 53 Mass. 428 (1847), on the New York stat-

short sales, was repealed by implication by the statute of 1868, declaring the sale to be valid though there be no consideration, or payment of a consideration, or no ownership by the vendor of such stock at the time of the sale. In England the statute of 1734,¹ prohibiting gambling in the public funds, was repealed in 1860.² It is evident from the history of these statutes against stock gambling that it is a difficult and delicate task to frame a statute that will cure an evil, which is manifest to all, and a statute also that will not interfere with the legitimate transactions which have for many years been producing our railways and developing the material resources of the country.³

§ 343. *Test of legality of stock transactions.*—Although, as already stated, stock sales, where no delivery, but merely a settlement of gain or loss is intended, are wagers; and although such wagers are void by the statutes of some States, and by the rules of public policy in others,⁴ yet difficulty is experienced in deter-

ute; *Staples v. Gould*, 9 N. Y. 520 (1854), criticising *Gram v. Stebbins*, 6 Paige, 124 (1836); *Frost v. Clarkson*, 7 Cowen, 24 (1827); *Cassard v. Heinmann*, 14 How. Pr. 84 (1856); *aff'd*, 1 Bosw. 207. In Arkansas a broker and others are liable criminally for doing business in futures. *Fortenbury v. State*, 1 S. W. Rep. 58 (1886).

¹ 7 Geo. II, c. 8, and 10 Geo. II, ch. 8. For cases under this statute, see *Hewett v. Price*, 4 Man. & Gr. 355 (1842); *Fisher v. Price*, 11 Beav. 194 (1848); *Mortimer v. McCullon*, 6 M. & W. 69 (1840); *Ellsworth v. Cole*, 7 M. & W. 30; *Byle on Bills*, 194; 2 *Kent's Com.* 468, n. (6). The statute did not apply to stock in private corporations. *Hibblewhite v. McMorine*, 5 M. & W. 462 (1839), overruling *Bryan v. Lewis*, R. & M. 386 (1826).

² 23 & 24 Vict., c. 28.

³ *Des Passos on Stock Brokers and Stock Exchanges* (1882), p. 405, says: "The history of these stock-jobbing acts seems to prove conclusively that they have never been effective in preventing speculations in stocks. In almost every instance in which they have been adopted, after lingering for years on the books, scorned and violated by 'the unbridled and defiant spirit of speculation,' despite the earnest efforts of the courts to enforce them, they have finally been repealed. It

is, perhaps, better to allow the evil to correct itself, as it surely does, than to bring the administration of justice into contempt by filling the books with useless laws, which are at all times openly violated and laughed at, and which seem hardly more effective to prevent the practice at which they are aimed than legislation directed against the laws of nature."

⁴ Particularly in Pennsylvania are such stock wagers void by public policy. *Worth v. Phillips*, 89 Penn. St. 250 (1879); *Farrier v. Gabell*, 89 Pa. St. 89 (1879); *Ruchizky v. De Haven*, 97 Penn. St. 202 (1881); *Dickson's Executor v. Thomas*, 97 Penn. St. 278 (1881). In the case, *Bruas' Appeal*, 55 Penn. St. 294 (1867), the court says: "It is said the form in which this contract appears enters largely into the business of stock brokerage. This is a mistake; the *bona fide* purchaser of stocks, no doubt, can be conducted in a legitimate way, and is so generally without trenching in the least on the gambler's province. If this be impossible, however, the fewer licenses that are issued for such business the better. Anything which induces men to risk their money or property without any other hope of return than to get for nothing any given amount from another, is gambling, and demoralizing to the community, no matter by what name it may be called."

mining whether the parties really intended to deliver the stock or to pay differences. The question of intent is always difficult of ascertainment and of positive proof. It is pre-eminently a question for the jury. It accordingly is found in most of the cases involving the question, whether the transaction was stock gambling, that the court submitted to the jury whether an actual delivery of the stock was intended or not. If not, then, as a matter of law, the transaction was a wager. If a wager, it is, by statute in some States, by public policy in others, a void transaction, and the parties have only the rights given them on void contracts.¹

§ 344. *When intent to deliver is question for the jury and when not.*—The question whether the parties to an executory sale of stock intended to actually deliver the stock, or merely to pay and receive the gain or loss, is for the jury.² In the application of this rule, however, great care is to be exercised in submitting the question and charging the jury. Thus, an “option,” “put,” “call,” “straddle,” or other similar stock exchange contract may be made with an intent to actually deliver the stock, and if so, is unobjectionable and is enforceable.³ The parties may be asked

¹ See §§ 345, 346. See also Greenhood on Public Policy, pp. 230–237.

² *Whitesides v. Hunt*, 97 Ind. 191 (1884); *Gregory v. Wendell*, 39 Mich. 337 (1878). And all the circumstances are to be taken into consideration. *Beveridge v. Hewitt*, 8 Bradw. 467 (1881); *Hawley v. Bibb*, 14 Reporter, 172 (1881); *Brand v. Henderson*, 107 Ill. 141 (1883); *Barnard v. Backhaus*, 52 Wis. 593 (1881); *Kirkpatrick v. Bonsall*, 72 Penn. St. 155 (1872).

³ For definitions of these terms see Ch. XXV. A “put” is not *per se* conclusive evidence of an intent not to deliver. *Bigelow v. Benedict*, 70 N. Y. 202 (1877). A “straddle” follows the same rule. The parties may have intended to deliver the stock. *Harris v. Tumbridge*, 83 N. Y. 92 (1880); *Story v. Salomon*, 71 N. Y. 420 (1877). *Cf. Ex parte Young*, 6 Biss. 53 (1874); *Webster v. Sturges*, 7 Bradw. 56 (1880); *Tenney v. Foote*, 4 Bradw. 594 (1879); *Lyon v. Culbertson*, 83 Ill. 33 (1876); *Gilbert v. Gouger*, 8 Biss. 214 (1878). A short sale is not *per se* a wager, nor is it presumed to be. *Maxton v. Gheen*, 75 Penn. St. 166 (1874); *Huss v. Rau*, 95

N. Y. 359 (1884); *Knowlton v. Fitch*, 52 N. Y. 288 (1873); *White v. Smith*, 54 N. Y. 522 (1874); *Cameron v. Durkheim*, 55 N. Y. 425 (1874); *Third Natl. Bk. v. Harrison*, 10 Fed. Rep. 243 (1882). These decisions rest upon the principle of law laid down in *Stanton v. Small*, 3 Sandf. (N. Y.) 230, that “a contract for the sale of goods, to be delivered at a future time, is not invalidated by the circumstances that at the time of the contract, the vendor neither had the goods in his possession, nor has entered into any contract to buy them, nor has any reasonable expectation of becoming possessed of them at the time appointed for delivery, otherwise than by purchasing them after making the contract.” There are many cases to the same effect. See *Noyes v. Spaulding*, 27 Vt. 420 (1855); *Shales v. Seigmoret*, 1 Ld. Raymond, 440 (1691); *Frost v. Clarkson*, 7 Cow. 25 (1827); *Dewey on Contracts for Future Delivery*, 97. *Thacker v. Hardy*, L. R., 4 Q. B. D. 685 (1878), holding that if the intent, at the time of buying, was to deliver, it is not a wager, even though that intent be afterwards changed. As to the legality of a “corner,” see § 348.

directly whether they intended that a delivery should be made.¹ If one party intended to have a delivery, the transaction is valid, even though the other party intended otherwise.² As between a party and his broker, however, greater difficulty arises, and in some jurisdictions, the intent between them governs their relations, irrespective of the intent of the party dealing with them.³ The fact that stock transactions were carried on by "margins" is no evidence that they were gambling contracts,⁴ excepting in Pennsylvania and New Jersey. In these States, this fact alone seems to be sufficient evidence of a wager.⁵ A wager contract is not proved by the fact that the party selling stock to be delivered at a future time, intends to purchase that amount of stock in time for the delivery, or *vice versa*.⁶ "An executory contract for the sale of goods for future delivery is not infected with the

¹ *Yerkes v. Saloman*, 11 Hun, 471 (1877); *Cassard v. Hinman*, 6 Bosw. 14; *First Natl. Bk. v. Oskaloosa*, 23 N. W. R. 255. *Ex parte Young*, 6 Biss. 53 (1874). In the case of *Porter v. Viets*, 1 Biss. 177 (1857), the court refused to admit parol evidence that the contract was gambling, for the reason that it varied a written contract.

² *Wall v. Schneider*, 17 Reporter, 700 (1884), where the court said, "We are not aware of any adjudicated cases going to the extent of holding that the mere secret intention of one party to the contract, not communicated to the other party, is sufficient to invalidate such contract." *Irwin v. Williar*, 110 U. S. 499 (1884). "A transaction which, on its face is legitimate, cannot be held void as a wagering contract by showing that one party only so understood and meant it to be. The proof must go farther, and show that this understanding was mutual." *Whitesides v. Hunt*, 97 Ind. 191 (1884); *Pixley v. Boynton*, 79 Ill. 351 (1875); *Lehman v. Strassberger*, 2 Woods (C. C.), 554 (1873). *Contra*, *Fareira v. Gabell*, 89 Penn. St. 89 (1879); *Beveridge v. Hewitt*, 8 Bradw. 467 (1881); *Conner v. Robertson*, Louisiana Sup. Ct. (1886), the court saying: "In order to affect the contract the alleged illegal intent must be mutual, the intent of one party, not communicated to or concurred in by the other, will not avail him."

³ See §§ 345, 346.

⁴ *Sawyer v. Taggart*, 14 Bush, 727 (1879); *Wall v. Schneider*, 17 Rep. 700 (1884); *Bartlett v. Smith*, 13 Fed. Rep. 263

(1882); *Whitesides v. Hunt*, 97 Ind. 191 (1884); *Union Natl. Bk. v. Carr*, 15 Fed. Rep. 238 (1883); *Hatch v. Douglas*, 48 Conn. 116 (1880). Many other cases do not directly pass on this question, but assume that the depositing of a margin, as a security to the broker, does not prove an intent not to have a delivery of the stock.

⁵ *Ruchizky v. DeHaven*, 97 Penn. St. 202 (1881); *Dickson v. Thomas*, 97 Penn. St. 278 (1881); *Fareira v. Gabell*, 89 Penn. St. 89 (1879); *Maxton v. Green*, 75 Penn. St. 166 (1874); *North v. Phillips*, 89 Penn. St. 250 (1879); *Flagg v. Baldwin*, 38 N. J. Eq. Rep. 219; *Justh v. Holliday*, 11 Wash. L. Rep. 418 (1883).

⁶ In the case of *Ashton v. Dakin*, 7 W. R. 384 (1859), the court held it not to be a wager contract to order a broker to buy stock "and let the bargain be so as to day of payment, that you may have an opportunity of reselling it for me by such a day, when I expect the market will have risen, and then you will pay the seller for me with the money you receive from the purchaser, and I shall receive the gain from you, if any, or pay you the loss." So also *Smith v. Bouvier*, 70 Penn. St. 325 (1872), holds that stocks bought and sold, upon speculation, are not necessarily wager contracts. A person may sell without owning the stock, and at time of delivery buy to deliver, and yet the transaction be not a wager, where the jury finds that there was an intent to deliver in both the selling and buying. See also *Thacker v. Hardy*, L. R., 4 Q. B. Div. 685 (1879); *Sawyer v. Taggart*, 14 Bush, 727 (1879).

quality of a wager by reason of the fact that at the date of the contract the vendor had not the goods; had not entered into any arrangement to provide them, and had no expectation of purchasing them, unless by a subsequent purchase in the market.¹ The financial responsibility of the parties,² and their other transactions in the same line,³ are admissible as evidence as to whether there was an intent to deliver the stock or merely to pay the gain or loss. The burden of proving that a stock transaction is a gambling contract is upon him who affirms it.⁴

§ 345. *Gambling stock contracts as affecting the relations between the principal and his broker.*—A broker is but an agent of his principal. As such he may hold the principal liable for commissions and for losses paid on stock transaction where those stock transactions are legitimate and legal. Where, however, the stock contracts are of a wager or gambling nature, a more difficult question arises, and the decisions are irreconcilable. In England, in 1878, Judge Lindley, in *Thacker v. Hardy*,⁵ a carefully considered case, held that where the principal has been carrying on gambling transactions, he cannot escape or repudiate his liabilities to his broker in those transactions, even though the latter knew of the gambling character of the business. The principal is liable to his broker as though the transactions were free from such objections. This is the well established rule in England.⁶

¹ *Conner v. Robertson*, Louisiana Sup. Ct. (1886), the court saying also that *Larymer v. Smith* (1 B. & C. 1) has been repeatedly overruled. See also, *supra*, page 356, note 3.

² *Kirkpatrick v. Bonsall*, 55 Penn. St. 155 (1872); *First Natl. Bank v. Oskaloosa P. Co.*, 23 N. W. Rep. 255 (1885). *In re Green*, 7 Biss. 338 (1877); *Beveridge v. Hewitt*, 8 Bradw. 467 (1881); *Justh v. Holliday*, 11 Wash. Rep. 418 (1883); *North v. Phillips*, 89 Penn. St. 250 (1879); *Patterson's Appeal*, 16 Rep. 59 (1883); *Flagg v. Baldwin*, 38 N. J. Eq. 219; *Colderwood v. McCrea*, 11 Bradw. 543 (1882).

³ *Kirkpatrick v. Bonsall*, 72 Penn. St. 155 (1872); *Beveridge v. Hewitt*, 8 Bradw. 467 (1881); *Irwin v. Williar*, 110 U. S. 499 (1884).

⁴ *Dewey on Contracts, &c.*, p. 207, says, "All the cases, except *Barnard v. Backhaus*, 52 Wis. 503; *Cobb v. Prell*, 15 Fed. Rep. 774; *Beveridge v. Hewitt*, 8 Bradw. 467; *Stebbins v. Leowolf*, 8 Cush.

137, and possibly *Chandler's Case, Ex parte Young*, 6 Biss. 53, hold that these contracts are presumed to be *bona fide*, and in order to show them to have been used as covers for wagers, an agreement to that effect must appear to have been made. According to these excepted cases option contracts are presumed to be invalid, and proof must be made that they are *bona fide*." See also *Dewey*, p. 46.

⁵ L. R., 4 Q. B. D. 685.

⁶ *Re Hart*, Weekly Notes, 85 (1870); *Cooper v. Neil*, 13 Weekly Notes, 128 (1878); *Ex parte Rogers*, L. R., 15 Ch. D. 207 (1879); *Faikney v. Reynons*, 4 Burr. 2069 (1767); *Jessopp v. Lutwyche*, 10 Ex. 614 (1854); *Knight v. Cambers*, 15 C. B. 562 (1855); *Knight v. Fitch*, 15 C. B. 566 (1855); *Lyne v. Siesfield*, 1 H. & N. 278 (1856); *Rosewarne v. Billing*, 15 C. B. N. S. 316 (1863); *Pidgeon v. Burslem*, 8 Ex. 465 (1849). *Contra*, *Byers v. Beattie*, 16 Weekly Rep. 279 (1868, Ex. Irish).

§ 346. In this country an opposite rule prevails for the most part. The great weight of authority holds that where the broker has knowledge of the purpose to gamble in stocks and aids in carrying out that purpose, he cannot recover for services rendered or losses incurred and paid by himself.¹ A few cases hold to the same effect as the English rule.² Many cases which seem to favor the English rule do so, only by *dicta*, inasmuch as the transactions involved in such cases are held not to be wager contracts.³ In Pennsylvania and New Jersey the American rule is rigidly enforced. The broker is held to be dealing as a principal, not as an agent in all stock gambling transactions.⁴ He cannot recover commissions nor losses.⁵ If his principal is an infant the broker is liable to such infant for all sums received by way of margins.⁶ If, however, the parties do not raise the question of the legality of the transaction, the court cannot.⁷ In Ohio, it is held, that the broker may be made to account for profits, even though the transaction was a gambling one.⁸ A note and mortgage given to the broker in settlement of a gambling transaction will not be interfered with.⁹ The broker is not liable for a sale of the stock, on

¹ *Irwin v. Williar*, 110 U. S. 499, 510 (1883); *McClellan v. Stuve*, 15 Mo. App. 317, per Thompson, J.; *Ream v. Hamilton*, 15 Mo. App. 377. *Cf.* *Kent v. Miltenberger*, 13 Mo. App. 503, 511 (1883). See also, as supporting above rule, *Everingham v. Meighan*, 5 Wis. Lg. News, 25 (1882). *In re Green*, 7 Biss. 338 (1877); *Bartlett v. Smith*, 13 Fed. Rep. 263 (1882); *Tenney v. Foote*, 4 Bradw. 594 (1879); *aff'd* 95 Ill. 99 (1880), defeating a note given to the broker; *Calderwood v. McRae*, 11 Bradw. 543 (1882); *Webster v. Sturges*, 7 Bradw. 56; *Barnard v. Backhaus*, 52 Wis. 533 (1881), defeating notes. *Beveridge v. Hewitt*, 8 Bradw. 467 (1881); *Whitesides v. Hunt*, 97 Ind. 191, 203 (1884); *Melchert v. American U. Tel. Co.*, 11 Fed. Rep. 193; *First Natl. Bk. of Lyons v. Oskaloosa Packing Co. (Iowa)*, 23 N. W. Rep. 255 (1885), holding a note void. *Stewart v. Garrett*, 4 Atl. Rep. 399 (Penn. 1886); *Stewart v. Schall*, 34 Alb. L. J. 98 (Md. 1886).

² *Brown v. Speyers*, 20 Gratt. (Va.) 296 (1871); *Wyman v. Fiske*, 85 Mass. 238 (1861), on the ground that the note sued on was a voluntary payment to the broker. *Warren v. Hewitt*, 45 Ga. 501 (1872); *Marshall v. Thurston*, 3 Lea

(Tenn.), 741 (1879), where also a note had been given. *Jackson v. Foote*, 12 Fed. Rep. 37, also a note case, the court saying, that as between the broker and his principal the decision probably would be different. *Cf. Tinsley's Case* (U. S. Ct. Ct.), 10 Fed. Rep. 249.

³ *Lehmann v. Strassberger*, 2 Woods, 554 (C. C. 1873); *Rumsey v. Berry*, 65 Me. 570 (1876); *Sawyer v. Taggart*, 14 Bush, 727 (1879); *Durant v. Burt*, 98 Mass. 161 (1867); *Williams v. Carr*, 80 N. C. 294 (1879).

⁴ *Ruchizky v. De Haven*, 97 Penn. St. 202 (1881).

⁵ *North v. Phillips*, 89 Penn. St. 250 (1879); *Flagg v. Baldwin*, 38 N. J. Eq. Rep. 219; *Fareira v. Gabell*, 89 Penn. St. 89 (1879), holding that notes given to the broker are void.

⁶ *Ruchizky v. De Haven*, *supra*.

⁷ *Gheen v. Johnson*, 90 Penn. St. 38 (1879); *Williams v. Carr*, 80 N. C. 294 (1879).

⁸ *Norton v. Blinn*, 39 O. St. 145 (1883).

⁹ *Clark v. Foss*, 10 Chicago Legal News (U. S. D. Ct. 1878). *Cf. Tatum v. West* (N. J.) Central Rep., March 25, 1886.

failure of margin, without notice to the principal, where the business is gambling.¹

§ 347. *Gambling stock transactions as affecting notes, bonds, mortgages, &c., growing out thereof.*—The penalty of engaging in a stock gambling operation is that, in case the transaction is declared by a court of justice to be illegal as a wager contract, the court declines to aid either party.² As a general rule all liability on the part of either party is unenforceable. Money paid by the principal cannot be recovered back.³ Neither principal can collect the gains of the transaction, and neither is liable for a loss.⁴ Notes given in settlement are void and not collectible,⁵ even in the hands of *bona fide* purchasers.⁶ Bonds and mortgages given in payment are void.⁷ Due bills,⁸ acceptances,⁹ and guaranties¹⁰ of notes are not valid or enforceable. If a part of the

¹ North v. Phillips, 89 Penn. St. 250 (1879).

² Reese v. Fermie, 13 W. R. 6 (1864), holding that the court will not aid one who has been tricked in gambling in stocks.

³ Gregory v. Wendall, 39 Mich. 337 (1878); Id. 40 Mich. 432 (1879); Wyman v. Fiske, 85 Mass. 238 (1861). Cf. Norton v. Blinn, 30 O. 145 (1883).

⁴ Grizewood v. Blane, 11 C. B. 526 (1851); Webster v. Sturges, 7 Bradw. (Ill.) 560 (1880); *Ex parte* Young, 6 Biss. 53 (1874); Thompson v. Cummings, 68 Ga. 124 (1881); Yerkes v. Solomon, 11 Hun, 471 (1877). A partner, however, may have contribution for losses paid at the express request of the other member of the firm. Petrie v. Hannay, 3 Term Rep. 418 (1789).

⁵ Barnard v. Backhaus, 52 Wis. 593 (1881); Fareira v. Gabell, 89 Penn. St. 89 (1879); Lowry v. Dillman, 18 N. W. Rep. (Wis.) 4 (1884); Justh v. Holliday, 17 Central L. J. 56 (1883); 11 Wash. L. Rep. 418; Cunningham v. Third, &c., Bk. of Augusta, 71 Ga. 400 (1883); Tenney v. Foote, 4 Bradw. 595 (1879), *aff'd* 95 Ill. 99. Cf. Wyman v. Fiske, 85 Mass. 238.

⁶ Barnard v. Backhaus, 52 Wis. 593 (1881); Steers v. Lashley, 6 Term Rep. 61 (1794); Tenney v. Foote, 4 Bradw. (Ill.) 594 (1879); Cunningham v. Nat'l Bank of Augusta, 71 Ga. 400 (1883); Lowry v. Dillman, 18 N. W. Rep. 4 (1884). An accommodation indorser to the note

may set it up. Justh v. Holliday, 17 Central L. J. 56 (1883); 11 Wash. Law Rep. 418. Note to bank is valid, though the proceeds were to pay a stock gambling debt and the bank knew that fact. Marshall v. Thurston, 3 Lea (Tenn.), 741 (1879). Cf. Cannon v. Bryce, 3 B. & A. 179 (1819).

⁷ Amory v. Merryweather, 2 B. & C. 573 (1824); Flagg v. Baldwin, 38 N. J. Eq. Rep. 219 (1884); Griffiths v. Sears, 112 Penn. St. 523 (1886); Barnard v. Backhaus, 52 Wis. 593 (1881). A judgment entered by confession on a bond given for a gambling debt may be set aside. Everitt v. Knapp, 9 Johns. 331 (1810); Beveridge v. Hewitt, 8 Bradw. 467 (1881). A court of equity will enjoin the transfer of a note and will decree the cancellation of a mortgage given by a married woman in payment of her husband's stock gambling debts. Tantum v. West (N. J.) Central Rep. March 25, 1886 (*aff'd*, it seems, Nov. 1886), but will not where given by the party himself to his brokers. Clark v. Foss, 10 Chicago Legal News (U. S. D. Ct. Wis. 1878).

⁸ Rudolf v. Winters, 7 Neb. 125 (1878).
⁹ Steers v. Lashley, 6 Term Rep. 61 (1794). Rawlings v. Hall, 1 Carr. & P. 11 (1823), holds that the broker on the witness stand need not admit that the consideration was a gambling debt, since it would subject him to a common law criminal prosecution.

¹⁰ Tenney v. Foote, 95 Ill. 99 (1880).

consideration is void the whole contract and all securities given thereunder are void.¹

§ 348. *Sales as affected by the legality of the purposes for which the stock is obtained.*—The courts will not aid either party in carrying out an agreement for advancing the price of stock by means of fictitious dealings designed to deceive others concerning the real value of such stock.² Where both the vendor and vendee of stock know that the purpose of the vendee is to control the corporation and illegally issue corporate paper, the sale is illegal and void.³ An agreement to make a "corner" in stock, by buying it up so as to control the market and then purchasing for future deliveries, is illegal.⁴ It is not necessarily unlawful to form a "pool" for the purpose of dealing in a particular stock.⁵ An agreement to hold stock and sell together is valid.⁶ In Massachusetts it is held that a contract by which a shareholder in a corporation agrees to secure to the purchaser of his stock a corporate office, at a stated salary, and in case of his removal to repurchase the stock, is void as against public policy and as a fraud on other stockholders, unless it is proved that the transaction is not for the private benefit of the vendor, or that it was consented to by the other stockholders.⁷ In New York, on the other hand, it is held that a contract to convey a majority of the stock of a corporation, and to procure the resignation of the corporate directors, thereby enabling the vendee to elect directors satisfactory to himself, is a valid and legal agreement.⁸ One railroad company cannot pur-

¹ *Tenney v. Foote*, *supra*. See also *Faireira v. Gabell*, 89 Penn. St. 89 (1879).

² *Livermore v. Bushnell*, 5 Hun, 285 (1875).

³ *Town Council, &c. v. Elliott*, 5 O. St. 113 (1855).

⁴ *Sampson v. Shaw*, 101 Mass. 145 (1869); *Raymond v. Leavitt*, 13 Cent. L. J. 110 (1881); *Morris Run Coal Co. v. Barclay Coal Co.*, 68 Penn. St. 173 (1871); *Arnot v. Pittston, &c., Coal Co.*, 68 N. Y. 558 (1877). *Cf. Petrie v. Hannay*, 3 Term R. 418 (1789). A person making a "corner" in stocks is not subject to a criminal prosecution therefor. *Raymond v. Leavitt*, 46 Mich. 447 (1881); *Barry v. Croskey*, 2 J. & H. 1 (1861), holding that the victim of the "corner" may file a bill in equity to recover back the money lost.

⁵ *Quincey v. White*, 63 N. Y. 370, 383

(1875), modifying *Quincey v. Young*, 5 Daly, 32 (1873).

⁶ *Havemeyer v. Havemeyer*, 11 J. & S. (N. Y.) 507 (1878); *Id.* 13 Id. 464; *aff'd* 86 N. Y. 618; *Griffith v. Jewett*, 15 Week. Law Bull. 419, an important case. But an agreement not to sell except by concurrent consent of all signers to the agreement, is void as in restraint of trade and against public policy. *Fisher v. Bush*, 35 Hun, 641 (1885).

⁷ *Guernsey v. Cook*, 120 Mass. 501 (1876); *Noyes v. Marsh*, 123 Mass. 286 (1877).

⁸ *Barnes v. Brown*, 80 N. Y. 527 (1880). *Contra, Jacobs v. Miller* (N. Y. Supr. Ct.), 15 Alb. L. J. 188 (1877); *Freemont v. Stone*, 42 Barb. 169 (1864). Where the agreement was to keep the vendor in a professorship the court will

chase a controlling interest in another railroad company for the purpose of managing or absorbing the latter, but this rule grows out of the fact that such purchases are beyond the powers of the corporation.¹ It is immaterial that the vendee already controls one railroad company and that the stock contracted to be sold will give him the control of another. He is entitled to the stock.² An agreement to contribute stock towards a common undertaking, is enforceable, the consideration being the mutual obligation.³ But the common undertaking must be a legal one.⁴

C.—FRAUD AS AFFECTING A SALE OF STOCK.

§ 349. *Extent of subject treated herein.*—In a previous chapter of this treatise the effect of fraud and fraudulent representations on a subscription for stock was fully treated. There is little difference in the principles of law governing fraud as affecting sales of stock, from fraud as affecting subscriptions for stock. Most of the cases assume that the same principles apply to both kinds of transactions. Consequently the questions of what constitutes fraud herein; what remedies the defrauded person has; and the general principles governing this branch of the law, will be fully understood only by a comparison of these two parts of this work.⁵

§ 350. *What has been held to constitute a fraud herein.*—It is difficult to lay down rules as to what does and what does not amount to fraudulent misrepresentations. The courts, consequently, let each case stand upon its own facts. Certain states of fact have, however, been passed upon as constituting fraud, and as such they aid in coming to a conclusion on facts in somewhat similar cases. Thus, it has been held to be a fraudulent misrepresentation to make false statements as to the location, explorations, and developed state of a mine;⁶ or that a patent owned by the company was of great value, and that certain other persons

not aid the parties. The agreement is against public policy. *Jones v. Scudder*, 2 Cin. Sup. Ct. 178 (1872).

¹ See § 315.

² *Havemeyer v. Havemeyer*, *supra*; *O'Brien v. Breitenbach*, 1 Hilt. 304. Cf. § 315, n. 6.

³ *Conrad v. La Rue*, 52 Mich. 83 (1888).

⁴ If the purpose is to rob a railroad

and bribe a judge, the court will aid no one. *Tobey v. Robinson*, 99 Ill. 202 (1881).

⁵ See Chap. IX. In the important case, *Western Bank v. Addie*, L. R. 1 H. L. (Sc.) 145, part of the shares had been subscribed for and part purchased. The court applied the same principle to both.

⁶ *Morgan v. Skiddy*, 62 N. Y. 319 (1875).

were owners of stock;¹ that the company was prosperous, when in fact large overissues of stock had been made;² or that the corporate property was free from incumbrance;³ or that the corporation would guarantee certain dividends;⁴ or any false statement or general fraudulent act, or fraudulent concealment of a material fact whereby the purchaser is induced to complete the sale of stock.⁵ It is not, however, a fraudulent representation to state that the capital stock is all paid in when it is not,⁶ or that the stock is worth its par value.⁷

§ 351. It is a fraud on the vendee of stock to sell him as paid up stock that which is not paid up, although issued as paid up, with the participation of the vendor.⁸ It is fraud in the vendor to represent that property is to be turned in by him to the corporation at a certain price and then to refuse to carry out the latter contract.⁹ Where the vendor agrees to sell at a value to be ascertained by an

¹ *Miller v. Barber*, 66 N. Y. 558 (1876).

² *Cazeaux v. Mali*, 25 Barb. 578 (1857).

³ *Southwestern R. R. Co. v. Papot*, 67 Ga. 775, 692 (1881), the court saying: "It is, we think, sufficient to show that the misrepresentation or suppression of fact was of such a nature as to prove that the property purchased was of no value to the purchaser for the purposes for which it was bought, or that it would be reasonable to suppose that the purchaser would not have contracted for it had he had knowledge of the existence of this defect."

⁴ *Gerhard v. Bates*, 20 Eng. L. & Eq. 129 (1853).

⁵ See further illustrations in Ch. IX. Declaring a dividend in good faith and sound discretion is not fraud by reason of its turning out to have been ill advised. *Burnes v. Pennell*, 2 H. of L. Cases, 497 (1849). A representation that the stock "is good property or investment and is about to make a dividend" is a false representation when untrue, and where the person taking the stock as executor from a preceding executor objected to receiving it on account of his doubt or ignorance as to its character. *Lawton v. Kittredge*, 30 N. H. 500 (1855). Representations that a corporate property is valuable and one of the best properties in Colorado, when in fact the company was a bubble company, raises a question of fraud for the jury to pass upon. *Bradley v. Poole*, 98 Mass. 169 (1867). The payment of an excessive and speculative price for stock is not fraud and is no ground for setting

the sale aside. *Moffat v. Winslow*, 7 Paige Ch. 124 (1838). The vendor warrants the title to the stock, but not its quality or value. *Allen v. Pegram*, 16 Iowa, 163 (1864). A sale of stock in a company formed to purchase a railroad cannot be set aside merely because its title to the railroad fails. *State v. North. La. & T. R. R. Co.* 34 La. Ann. 947 (1882). In the case, *Wright's Appeal*, 99 Penn. St. 425 (1882), it was held that the corporation was not liable for the conversion of stock by its president, who obtained the certificates indorsed in blank from the owner on false representations that the corporation wished to use them. *Newlands v. National, &c., Association*, 53 L. T., N. S., 242 (1885); *March v. Eastern R. R. Co.* 43 N. H. 515 (1862), holding that the fact that the earnings were not distributed by dividends until after a sale of stock, does not constitute fraud. A confidential agent who uses his position to obtain stock of which the principal has been deprived wrongfully, must turn it over to the principal. *Hardenburgh v. Bacon*, 33 Cal. 356 (1867).

⁶ *Nelson v. Luling*, 62 N. Y. 645 (1875); *aff'd*, 4 J. & S. 544.

⁷ *Union Nat'l Bk. v. Hunt*, 76 Mo. 439 (1882).

⁸ *Sturges v. Stetson*, 1 Biss. 246 (1858), holding that the vendee is not liable on a note given in payment thereof. *Fosdick v. Sturges*, 1 Biss. 255 (1858), holding that the vendee may recover back money paid.

⁹ *Seaman v. Low*, 4 Bosw. 337 (1859).

examination of the corporate books and affairs, it is fraud in the vendee to cause false memoranda to be made by the employees of the corporation.¹ It is not fraud, however, for a director or other corporate officer to buy or sell stock at a profit due to his official knowledge of the condition of the corporation;² nor to obtain the stock by a threat of a call.³ The fact that a check given in payment for stock is not honored, although the money is in bank, is not fraud where payment was refused because of other frauds of the vendor;⁴ nor is it fraud to issue certificates before anything has been paid thereon, there being no participation by the vendor.⁵ It is fraud, however, to represent the company as having a full paid capital stock, when in fact the stock was wholly issued in payment of a worthless mine. The person making such representation is liable to the vendee.⁶

§ 352. *Fraud may be by corporate reports or prospectus.*—

A report of corporate officers to the stockholders, setting forth the condition of the affairs of the corporation, is deemed to be a statement to the public also, and it may be relied upon by any one in purchasing shares. This principle of law was first clearly enunciated in England in 1860, in the case of *Davidson v. Tulloch*.⁷ It was there held that there need be no privity between the officers issuing the report, and the person purchasing shares of stock from third persons. If such purchaser made his purchase relying upon material statements in corporate reports, which were false, he has his remedy against all persons, who knowingly made or issued the report.⁸ The leading case in this

¹ *Hager v. Thompson*, 1 Black, 80 (1861).

² *Board of Com'rs of T. Co. v. Reynolds*, 44 Ind. 509 (1873), and see § 320.

³ *Grant v. Attrill*, 11 Fed. Rep. 469 (1882). As to other cases of fraud by the vendee, see *Johnson v. Kirby*, 65 Cal. 482 (1884); *Hempling v. Burr*, 26 Northw. Rep. 496 (Mich. 1886).

⁴ *Comins v. Coe*, 117 Mass. 45 (1874).

⁵ *Woodruff v. McDonald*, 33 Ark. 97.

⁶ *Cross v. Sackett*, 2 Bosw. (N. Y.) 617 (1858). But an assertion that the capital stock is a certain amount, is not an assertion that it has all been paid in. *Colt v. Woollaston*, 2 P. Wms. 154 (1723).

⁷ 6 Jur. (N. S.) 543; s. c. 3 Macq. (H. of L.) 783.

⁸ *Scott v. Dixon*, 29 L. J. (Ex.) 62, n., explained in *Peek v. Gurney*, L. R., 6 H.

L. 398, as follows: "The report, though originally made to the shareholders, was intended for the information of all persons who were disposed to deal in shares, and the representation must be regarded as having been made not indirectly, but directly to each person who obtained the report from the bank where it was publicly announced it was to be bought, in the same manner as if it had been personally delivered to him by the director." *Gerhard v. Bates*, 20 Eng. L. & Eq. 129 (1853); *Cullen v. Thompson*, 6 L. T. (N. S.) 870 (1862), holding that where directors of a joint-stock company issue false and fraudulent reports to the public, and the manager, secretary, and other officers of the bank supply the detailed statements for such report, knowing them to be false and that they are to be used for purposes

country, on the liability of corporate directors, for fraudulent representation as to the condition of the company, not made to a purchaser of stock personally, but to the public generally, is *Cross v. Sackett*,¹ decided in 1858, where fraudulent dividends and representations based thereon were made.

§ 353. A somewhat different rule prevails in England, as to false statements contained in a prospectus of a corporation. A prospectus is issued for the purpose of inducing persons to subscribe for stock. Its object is not to promote the sale of that stock. Accordingly, it was decided, in *Peek v. Gurney*,² in 1873, that "the purchaser of shares in the market, upon the faith of a prospectus which he has not received from those who are answerable for it, cannot, by action upon it, so connect himself with them as to render them liable to him for the misrepresentation contained in it, as if it had been addressed personally to himself." In New York, a directly opposite rule prevails. In the case *Morgan v. Skiddy*,³ in 1875, the Court of Appeals held that: "If the plaintiff purchased his stock relying upon the truth of

of deceit, and a third party, acting on such reports, purchases shares in the company and suffers loss thereby, each of the officers of the company who knowingly assisted in the fraud is personally liable to such third party for the loss caused by such misrepresentation in the report, though the report was signed only by the directors and not by the subordinate officers.

¹ 2 Bosw. 617; 6 Abb. Pr. 247; 16 How. Pr. 62, the court saying: "When an instrument is made to deceive the public generally, and is adapted as well as intended to deceive some portion of the public, and as well one person as another, and is used as it was designed it should be, and fraudulently induces some one to act to his prejudice, by acting in the mode it was intended to influence them to act who might be deceived by it, the person who made the instrument and caused it to be thus fraudulently used, is liable to the person who has been defrauded by it. In such a case, the person injured has been subjected to damages by his fraudulent acts, and the fraudulent wrong-doer is liable for the consequences." *Cazeaux v. Mali*, 25 Barb. 578 (1857). "It is not essential that the reference should be addressed directly to the plaintiff, if it were made with the intent of its influencing

every one to whom it might be communicated, or who might read or hear of it, the latter class of persons would be in the same position as those to whom it was directly communicated, but they must have come to a knowledge of it before their purchase." *Morse v. Swits*, 19 How. Pr. 275 (1859), holding a bank officer liable for false statements in a report, published in accordance with the requirements of a statute. The court said: "Being published, the public or any individual of the public, has a right to believe it. And, if believing it any one of the public acts on that belief, the makers and publishers of this falsehood are to be held liable for the consequences they have caused" (citing cases). See also *Salmon v. Richardson*, 30 Conn. 360 (1862).

² L. R., 6 H. L. 377, overruling *Seymour v. Bagshaw*, 18 C. B. 903, and *Bedford v. Bagshaw*, 4 H. & N. 538; explaining *Scott v. Dixon*, 29 L. J. (Ex.) 62, n.; and *Gerhard v. Bates*, 2 El. & Bl. 476 (1853), and itself explained in *Cargill v. Bower*, L. R., 10 Ch. D. 502 (1878). In *Bellairs v. Tucker*, L. R., 13 Q. B. D. 563 (1884), the court seems to have assumed a different position, and to have treated the prospectus the same as any other method of misrepresentation.

³ 62 N. Y. 319.

the prospectus, he has a right of action for deceit against the persons who, with knowledge of the fraud and with intent to deceive, put it in circulation. The representation was made to each person comprehended within the class of persons who were designed to be influenced by the prospectus; and when a prospectus of this character has been issued, no other relation or privity between the parties need be shown, except that created by the wrongful and fraudulent act of the defendants in issuing or circulating the prospectus, and the resulting injury to the plaintiff."

§ 354. *Remedies for the fraud.*—There are two methods by which a person who has been fraudulently induced to buy or sell stock may remedy the wrong.¹ He may bring an action at law for damages for the deceit, or he may file a bill in equity to have the transaction set aside. The first named remedy is the most difficult, and the last the most easy to maintain.

§ 355. *Action for deceit.*—In order to sustain an action for damages for deceit, whereby plaintiff was induced to buy or sell shares of stock, it is necessary for the plaintiff to prove that statements were made or acts done which were fraudulent, that the person guilty of them knew that they were fraudulent, and that the plaintiff acted on such statements or acts in buying or selling the stock.² In England, a statement made recklessly or without regard as to whether it is true or untrue, may constitute a fraudulent intent.³ In New York, the rule is more stringent.

¹ In the case, *Smith v. Tracy*, 36 N.Y. 73 (1867), the vendee sued the vendor for a breach of warranty, alleging that the vendor's agent made certain representations as to the condition of the corporation. The action failed on the ground that the vendor did not authorize the agent to make a warranty. In the case *Ayres v. French*, 41 Conn. 142 (1874), the court held that fraud, inducing the owner of stock to part with it, may be remedied by the action of trover with a count in case for a fraudulent procurement and conversion of the stock. In the case, *National Exchange Co. v. Drew*, 2 Macq. (H. of L.) 103 (1855), it was held that where a person is induced by the fraudulent reports and representations of corporate officers to purchase stock, and the corporation loans him money to do so, it

cannot recover back the money loaned. See *Lightfoot v. Creed*, 8 Taunt. 267 (1818), holding that the vendee should declare not for money paid, but specially on the contract.

² *Arkwright v. Newbold*, L. R., 17 Ch. D. 301 (1881); *Arthur v. Griswold*, 55 N. Y. 400, 410 (1874), the court saying: "The rules of law require a reasonable degree of certainty as to each requisite necessary to constitute the cause of action, viz., representations, falsity, *scienter*, deception, and injury."

³ *Peek v. Gurney*, L. R., 6 H. L. 377, the court saying: "It is said that the prospectus is true as far as it goes, but half a truth will sometimes amount to a real falsehood." See also Ch. IX, § 147. In *Bellaires v. Tucker*, L. R., 13 Q. B. D. 563 (1884), however, the court says:

The case of *Wakeman v. Dalley*¹ applies to this class of cases the rule that "an action founded upon the deceit and fraud of the defendant cannot be maintained in the absence of proof that he believed, or had reason to believe at the time he made them, that the representations made by him were false, and that they were for that reason fraudulently made, or that he assumed or intended to convey the impression that he had actual knowledge of their truth, though conscious that he had no such knowledge."

This case held that a director is not liable for false representations on the company's printed business cards, of which he was ignorant, even though his name was attached thereto. In California, it is held that the purchaser of stock who has given a note in payment, cannot defeat an action on the note by setting up that the purchase was induced by fraud. He must first disaffirm the contract and return the certificate, and such return must be made before the trial.² But where the purchaser brings an action for deceit, he need not return the consideration nor rescind the contract.³ His injury is to be duly measured, and credit may be given for the real value of the stock.⁴ A director

"The action is one for deceit. It is necessary not only to prove that the statements in a prospectus or any other document are not true, but it must be proved that they are fraudulently put forward with intent to deceive."

¹ 51 N. Y. 27 (1872); *Nelson v. Luling*, 4 N. Y. Sup. Ct. 544 (1873); *aff'd* 62 N. Y. 645, the court below saying, an intent to deceive must be proved. "This intent may be inferred from evidence showing that the party making them knew of their falsity at the time, or at least professed knowledge of their truth when in point of fact he was conscious that he had none. But in either case, falsehood uttered with intent to deceive is essential. The presumption is in favor of innocence, and on that account, the intent or design to deceive the plaintiff must be affirmatively made out by evidence." But in the late and important case of *Schwenck v. Naylor*, 102 N. Y. 638 (1886), the court, per Rapallo, J., clearly enunciates the law as follows: "A false and fraudulent representation, as to the property of a corporation, of material facts which necessarily affect the value of shares of stock therein, constitutes a cause of action against a party inducing another, by means of such fraudulent misrepresentations, to pur-

chase such shares, quite as sufficient as if the purchase had been of the property of the company, with regard to which the representation was made; nor is it material in either case, that the purchase price of the property, or the money advanced on the faith of the representation, be paid to the party making it, for his individual benefit. If known to be false, and made with intent to deceive and defraud the person who is thereby induced to pay out his money, the person guilty of the fraud is liable to respond in damages, on the same principle on which one person is held liable in damages for fraudulently giving a false recommendation by which another is induced to give credit to a third party." See also *Clark v. Edgar*, 84 Mo. 106 (1884); *Gee v. Moss*, 12 Eng. & Am. Corp. Cas. 123 (Iowa, 1886). The action for deceit does not lie against the corporation, at least where no fraudulent intent is proved. *Pinedo v. Germania, &c., Co.*, N. Y. Daily Reg., July 29, 1885. See also § 157.

² *Gifford v. Carhill*, 29 Cal. 589 (1866).

³ *Miller v. Barber*, 66 N. Y. 558, 564 (1876); *Newbery v. Garland*, 31 Barb. 121 (1860).

⁴ See Ch. XXXV.]

is not liable for the misrepresentations and frauds of his co-directors, unless he has expressly authorized or tacitly permitted its commission.¹ The mere fact of being a director "is not *per se* sufficient to hold a party liable for the frauds and misrepresentations of the active managers of a corporation. Some knowledge of and participation in the act claimed to be fraudulent must be brought home to the person charged."² Where, however, proof is given, tending to show that the defendants were jointly engaged in a common scheme to defraud the plaintiff, the acts and declarations of one are admissible in proof against all,³ and frauds of a similar nature, at or near the same time as the one complained of, may be shown.⁴ The fraud practiced need not have been the sole inducement to the purchase.⁵ A party may be liable herein, although he was neither a corporate officer nor the vendor of the stock. If, with intent to cheat and defraud the vendee, he induces him, by fraudulent means, to purchase stock for value, which he knows to be worthless, he is liable for the damages sustained, although the purchase is actually made from another.⁶

§ 356. *Remedy in equity*.—A court of equity has concurrent jurisdiction with a court of law in enabling a purchaser of stock to recover back money paid, where the purchaser was induced by fraud chargeable to the vendor.⁷ In England, this remedy is held to be "precisely analogous to the common law action for deceit," in that damages may be awarded;⁸ the remedy, however, in equity, for a sale or purchase of stock induced by fraud, is by a bill to set aside the whole transaction.⁹ This remedy

¹ Weir v. Barnett, L. R., 3 Ex. D. 32.

² Arthur v. Griswold, 55 N. Y. 400, 406 (1874); Morgan v. Skiddy, 62 N. Y. 319.

³ Miller v. Barber, 66 N. Y. 558, 567 (1876).

⁴ Id.

⁵ Morgan v. Skiddy, 62 N. Y. 319, 328, and see Ch. IX.

⁶ Hubbell v. Meigs, 50 N. Y. 480, 490 (1872).

⁷ Hill v. Lane, L. R., 11 Eq. 215, where the court says: "It is so well settled that this court will entertain jurisdiction in such cases, that it would be a misfortune indeed to the public if there were any sufficient ground for considering that the jurisdiction is doubtful. . . ."

Although courts of common law may have jurisdiction in some such cases, there is clearly concurrent jurisdiction in this court," doubting Ogilvie v. Currie, 37 L. J. (Ch.) 541; Campbell v. Fleming, 1 Ad. & El. 40 (1834).

⁸ Peek v. Gurney, L. R., 5 H. L. 377, 390 (1873), the court saying, also: "There can be no doubt that equity exercises a concurrent jurisdiction in cases of this description, and the same principles applicable to them must prevail both at law and in equity."

⁹ Stainbank v. Fernley, 9 Sim. 556 (1839), where a sale by a director who has issued false reports, and declared illegal dividends was set aside. The corporation is a proper party to such ac-

follows the rules usually prescribed in such suits. It is not necessary for the complainant to prove a fraudulent intent. Innocent acts or misrepresentations suffice for this purpose, where they would be insufficient to sustain an action for deceit.¹

Where, however, the fraud is chargeable to the corporate officers or third persons, and the vendor of the stock is innocent, the vendee cannot rescind the sale.² Equity will sometimes compel the vendor to make good his representations. Thus where the vendor represented that the corporate property was unincumbered, equity will at the instance of the purchaser of stock enjoin the vendor from enforcing a lien which he has on such property.³ The right to rescind the contract for fraud is waived by taking a bond of indemnity against liability on the stock, such bond being taken upon discovery of the fraud.⁴ The purchaser repudiating the transaction must tender back the stock received by him.⁵

§ 357. *Fraud in selling stock may amount to a conspiracy.*

—A combination of persons, to fraudulently raise the price of a stock by misrepresentations and fraudulent practices, may amount to a criminal conspiracy. In England, in 1858, the directors of a joint-stock bank were found guilty of a conspiracy to defraud, where, knowing the bank to be insolvent, they issued a balance sheet showing a profit, and declared a dividend, and issued advertisements inviting the public to invest on such representations.⁶

tions, if a registry has been obtained by the person who has obtained the stock by fraud, since a retransfer on the corporate books is asked for. See also *Bradley v. Luce*, 99 Ill. 234 (1881); *Johnson v. Kirby*, 65 Cal. 482 (1884).

¹ *Arkwright v. Newbold*, L. R., 17 Ch. D. 301 (1881).

² *Moffat v. Winslow*, 7 Paige, 124 (1838).

³ *Jones v. Bolles*, 9 Wall. 364 (1869).

⁴ *Bridge v. Penniman*, 51 Superior Ct. (N. Y.) 183 (1885).

⁵ *Francis v. New York & B. El. R. R. Co.*, 17 Abb. N. C. (N. Y.) 1 (1885).

⁶ *Regina v. Brown et al.*, 7 Cox's Criminal Cases, 442 (1858); *Regina v. Esdaile*, 1 F. & F. 213 (1858). There cannot be such an offense against the United States by the directors of a national bank, since the offense is not recognized by statute. *United States v. Britton*, 108 U. S. 199 (1883).

CHAPTER XXI.

SALES OF STOCK.—MISCELLANEOUS RIGHTS OF THIRD PARTIES.

A.—PURCHASES WITHOUT A CERTIFICATE OF THE STOCK.

- § 358. Rights of a purchaser of certificate of stock where the corporation has registered transfer to another without surrender of certificate.
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- § 363. Forgery as affecting a sale of stock.
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§ 371 E.—CONFISCATION OF STOCK.

A.—PURCHASES WITHOUT A CERTIFICATE OF THE STOCK.

§ 358. *Rights of a purchaser of certificate of stock where the corporation has registered transfer to another without surrender of certificate.*—It has often happened that an owner of stock, after selling his stock and delivering to the vendee the certificate therefor, indorsed in blank, has gone to the corporation before such transfer is registered, and by misrepresentation or other fraudulent means induced the corporation to issue to another purchaser a new certificate of stock without a surrender of the old one. It is the duty of the corporation to refuse to register a transfer unless the old certificate is delivered up. The outstanding certificate is a continuing affirmation by the corporation that no registry of a transfer of the stock represented by that certificate will be allowed until the certificate itself is presented and surrendered. This affirmation is sometimes declared in a by-law,¹ and sometimes it is printed on the face of the certificate itself.² The obligation of

¹ Bridgeport Bk. v. New York & N. H. R. R. Co., 30 Conn. 231 (1861); Strange v. Houston & T. C. R. R. Co., 53 Tex. 162

(1880); New York & N. H. R. R. Co. v. Schuyler, 34 N. Y. 30 (1865).

² Cushman v. Thayer Mfg. Co., 76 N. Y. 365 (1879).

the corporation, however, to require a surrender of the old certificate upon obtaining a registry, is the same whether there is a by-law, or a statement on the certificate, or neither of these. It exists without any express declaration or agreement.¹

§ 359. *Liability of the corporation herein.*—It is the duty and right of a corporation to refuse to allow a registry of a transfer of stock unless the outstanding certificate representing that stock be delivered up and cancelled. And it is a duty which the corporation is bound to fulfill. If it allows a transfer to be registered without the old certificate being produced and surrendered, it is liable to any person who, without notice, purchases or has purchased the outstanding certificate.² This rule is well estab-

¹ *Factors & T. Ins. Co. v. Marine D. D. & S. Co.*, 31 La. Ann. 149 (1879).

² *Id.*, where a pledgee recovered damages against the corporation for issuing new certificates without a surrender of the one which the plaintiff held. *Smith v. American Coal Co.*, 7 Lans. 317 (1873), where an unrecorded transferee recovered damages against corporation for issuing certificate to purchaser at execution sale on attachment against the transferor. See Chapter on Attachment and Execution. *Cushman v. Thayer Mfg. Co.*, 76 N. Y. 365 (1879), the court saying: "Any act suffered by the corporation that invested a third party with the ownership of the shares, without due production and surrender of the certificate, rendered it liable to the owner; and it was its duty to resist any transfer on the books without such production and surrender." *Bank v. Lanier*, 11 Wall. 369 (1870), the court saying: "It is equally clear that the bank, in allowing this stock to be transferred to other parties while the certificates were outstanding in the hands of *bona fide* holders, was guilty of a breach of corporate duty," and is liable. *New York & N. H. R. R. Co. v. Schuyler*, 34 N. Y. 30, 81 (1865); *Holbrook v. New Jersey Zinc Co.*, 57 N. Y. 616 (1874), the court saying: "It cannot be denied that if a corporation having power to issue stock certificates does in fact issue such a certificate, in which it affirms that a designated person is entitled to a certain number of shares of stock, it thereby holds out to persons who may deal in good faith with the person named in the certificate, that he is an owner and has capacity to transfer the shares. This proposition does

not rest on any view of the negotiability of stock, but on the general principles appertaining to the law of estoppel." *Moore v. Citizens Natl. Bk.*, 111 U. S. 156 (1883), where the court seems to hold that the person receiving new certificates without requiring a surrender of the old ones, is not such a *bona fide* transferee of stock as may hold the corporation liable. *Brisbane v. Delaware, L. & W. R. R. Co.*, 94 N. Y. 204 (1883); aff'g 25 Hun, 438, and holding that, until the purchaser of the outstanding certificates presents them, the corporation is protected in paying dividends to the transferee without the old certificates. If no certificate has been issued, the rule does not apply. *First Natl. Bk. v. Gifford*, 47 Iowa, 575 (1877). The unregistered holder of the certificates is protected, since, if he were obliged to notify the corporation at the time he purchases the stock, "the value of these certificates as a basis of credit would be greatly impaired, particularly where the pledge is made at a distance from the domicile of the corporation." *Smith v. Crescent City, & Co.*, 30 La. Ann. 1378 (1878); *Bridgeport Bk. v. New York & N. H. R. R. Co.*, 30 Conn. 231 (1861), the court saying: "The *bona fide* holders of such certificates had a right to rely on the certificate, under the circumstances, as securing to them the stock which they represented against all other parties." *Strange v. Houston & T. C. R. R. Co.*, 53 Texas, 162 (1880), on the ground that the non-production of the original certificate "is notice to the company that a superior title may be in a third party." *Lee v. Citizens Natl. Bk.*, 2 Cin. Sup. Ct. 298 (1872), holding that

lished, and is based on the usages and requirements of trade, and on a wise public policy which favors the protection of those who invest their money in certificates of stock, relying upon the corporation to protect the holder of that certificate.¹ Thus the corporation has been held liable where seventeen years have elapsed since a new certificate was obtained, on the ground that the outstanding certificate has been lost.² The corporation need not assume any risk, but may refuse to permit a registry on its books of the transfer unless the old certificate is produced and surrendered.³ Where, however, the corporation is compelled to

the holder of the old certificates is entitled to have the illegal registry cancelled. In England there seems to be no decision directly in point. A *dictum*, however, in *Shropshire U. Ry. & Canal Co. v. Queen*, L. R. 7 H. L. 496, 509 (1875), does not support the rule which prevails in this country. The court said, whether a transfer of shares in a company can or cannot be made without the production of the certificates of the shares is "entirely within the discretion of the directors. They were not bound to permit a transfer without the production of the certificate, but though not bound to permit a transfer, I apprehend they would not be in any way answerable if the transfer should be in any case made without the production of the certificates of the shares." The case of *Hart v. Frantino, &c., Gold Min. Co.*, L. R. 5 Ex. 111 (1870), holds, however, that where the corporation cancels the stockholdership of one who purchased after registry without a surrender of the old certificates having been obtained, he may hold it liable in damages. As between two unrecorded transfers, one having the certificate and the other, a subsequent purchaser, not having it, the former prevails. *Societe Gen. v. Tramways Union Co.*, L. R. 14 Q. B. D. 424 (1884).

¹ *Factors & T. Ins. Co. v. Marine D. & S. Co.*, 31 La. Ann. 149 (1879), the court saying: "We think that by thus making stocks transferable by mere delivery of the certificate, the law has intended to interdict corporations from transferring stocks on their books, except upon surrender of the certificate or upon proof of its loss or destruction. These certificates of stock have become such important factors in trade and credit that the law has intended to surround those who take them with the safeguards it accords to the holders of the other great

agencies of commerce—bills, notes, bills of lading, &c."

² *Cleveland & M. R. R. Co. v. Robbins*, 35 O. St. 483 (1880). But is not liable for dividends paid in the meantime. It was held further, that a by-law allowing such issue of new certificates in case of loss, had no effect as regards the plaintiff, and that the Statute of Limitations ran against the plaintiff only from the time he had notice of the new certificate. By statute, in New York, the person claiming to have lost his certificate may be compelled to give a bond of indemnity to the corporation before obtaining new certificates, and a holder of the old certificates may have the benefit of this bond. N. Y. Session Laws, 1873, ch. 151. See § 370. Such a subrogation was refused in *Greenleaf v. Ludington*, 15 Wis. 558 (1862).

³ The corporation may refuse to issue stock to the heirs of a stockholder unless they surrender the old certificates. *State v. New Orleans & C. R. R. Co.*, 30 La. Ann. 308 (1878); *National Bk. of New London v. Lake S. & M. S. R. R. Co.*, 21 O. St. 221 (1871), where the corporation refused to allow registry by a purchaser at an execution sale, although it was quite plain that the judgment debtor's sale of the certificates had been in fraud of creditors. As between two unregistered transferees, the one with the certificate is entitled to the stock, especially where he purchased first. *Maybin v. Kirby*, 4 Rich. Eq. (S. C.) 105; *Societe Generale de Paris v. Walker*, L. R. 11 H. of L. 20; aff'g L. R. 14 Q. B. D. 424. So also as between a *bona fide* purchaser, to whom the certificates are transferred, and a third party, to whom the vendor had given the stock previous to the sale, the vendee with the certificates is protected. *Crawford v. Dox*, 5 Hun, 507 (1875).

make the registry by legal proceedings, as in case of execution sales, it cannot be held liable to the holder of the outstanding certificate.¹ The corporation, when sued by the holder of the old certificate, is required either to replace the stock which has wrongfully been taken from the plaintiff, or it is obliged to compensate him in damages.

§ 360. *Rights of purchaser of stock without certificates.*—

A purchaser of stock who does not receive the certificates of the stock he has purchased, but who, nevertheless, obtains a registry on the corporate books, and receives new certificates without a surrender of the old, and who sells the new certificates, is not liable in damages to the holder of the old certificates.² The remedy of the latter is against the corporation, or he may sue the corporate officer who allowed the transfer.³ The purchaser of the stock may insist on the old certificate being produced and surrendered at the time of registration, but if he waives this right, and a registry is made, he cannot afterwards refuse to accept the stock on that account.⁴ The corporation is not liable to the person who is registered as a stockholder without a surrender of the old certificate, at least not where the registry is by the secretary, without special authority from the board of directors.⁵ Where, however, the purchaser of stock without the certificates obtained registry on the corporate book, the corporation cannot afterwards remove his name in favor of the purchaser of the old certificate. The former may compel the corporation to replace his name.⁶

¹ *Friedlander v. Slaughter House Co.*, 31 La. Ann. 523 (1879). See also Chap. XXII, § 388.

² *Baker v. Wasson*, 53 Texas, 150 (1880). Unless he obtained registry with knowledge that his vendor had already sold the old certificates to another. *Scripture v. Franchetown Soapstone Co.*, 50 N. H. 571 (1871).

³ *Baker v. Wasson*, 59 Texas, 140 (1883).

⁴ *Boatmen's Ins. & Trust Co. v. Able*, 48 Mo. 136 (1871).

⁵ *Hall v. Rose Hill & E. Road Co.*, 70 Ill. 673 (1873); *Houston & T. C. Ry. Co. v. Van Alstyne*, 56 Tex. 439 (1882), holding that the corporation is not bound to recognize as a stockholder one who obtains registry without a surrender of the

old certificates, a regular registry with a surrender of such certificates having previously been obtained by another. *Cf. Hart v. Frantino, & Co.*, 22 L. T. (N. S.) 30.

⁶ *Cady v. Potter*, 55 Barb. 463 (1869). In *Platt v. Birmingham Axle Co.*, 41 Conn. 255 (1874), the corporation was protected by its lien, and the fact that it bought the stock without the certificates was not the essential point of the case. The corporation cannot interplead after it has allowed the transfer. *Cady v. Potter, supra*; *Mt. Holly L. & M. T. Co. v. Ferrie*, 17 N. J. Eq. 117 (1864), but it may interplead if it has refused to transfer to any one. *Merchants Natl. Bk. v. Richards*, 6 Mo. App. 454 (1879).

B.—SUITS AFFECTING SALES OF STOCK.

§ 361. *Legal proceedings as affecting sales of outstanding certificates of stock.*—It is a well established principle of law that shares of stock may, for certain purposes, have a *situs* at two separate places at the same time. For the purposes of suits concerning rights to its title, for taxation, and for a few other purposes, shares of stock follow the domicile of the stockholder.¹ On the other hand, it has, at the same time, a *situs* where the corporation exists, and this *situs* may be for the purposes of suits concerning the title to the stock, for attachment and execution, and for various other similar purposes. Great difficulty arises in many instances of legal proceedings affecting the title to stock by reason of the fact that where the defendant has in his possession the certificates of stock, and is not enjoined from transferring them, he may transfer them, either before or during or after suit has been commenced against him to obtain possession of the stock represented by such certificates, or to subject it to his debts. The question then arises whether the *bona fide* transferee of such stock is to be allowed to retain the stock, or whether the successful plaintiff in the suit against the defendant who has transferred the stock, may follow such stock and take it from the transferee. This conflict of right between the purchaser of outstanding certificates and the purchaser whose title is based on judicial proceedings, arises most often in cases of attachment or execution issued against shares of stock, at the domicile of the corporation. In such cases the better rule seems to be that transferees of the certificate held by the defendant, are protected and entitled to protection at the hands of the corporation, if their purchase is made before the attachment or execution is levied, but that transfers made after levy are utterly void so far as the corporation and the plaintiffs to the suit are concerned, provided the suit itself is successful.² The same difficulty and conflict of rights arise in suits to reclaim stock, which has been taken from the plaintiff by fraud, or by the torts of an agent or pledgee, or by the breach of trust of an executor, administrator, guardian, or trustee.³ The plain-

¹ *Certificates of stock* have no *situs* or domicile. They cannot be attached or subjected to execution. The stock itself does not follow the certificate representing it. *Winslow v. Fletcher*, 4 Atl. Rep. 250 (Conn. April, 1886).

² *Smith v. American Coal Co.*, 7 Lans. 317 (1873); *Smith v. Crescent City, &c. Co.*, 30 La. Ann. 1378 (1878), and Chapter on Attachment and Execution.

³ *Holbrook v. New Jersey Zinc Co.*,

tiff seeking to recover his stock, certificates for which are in the hands of the defendant, seems to have but two modes of procedure whereby he may prevent the defendant from transferring the certificates. The suit should be brought in the State of the domicile of the corporation and attachment against the stock issued,¹ or when the defendant is sued in another State, an injunction restraining the defendant from transferring the stock should be obtained. It is true that after judgment has been obtained and the decree of the court executed, any subsequent transfer of the certificates by the defendant is null and may be disregarded by the plaintiff and by the corporation.² But while the suit is pending the defendant may transfer the certificates and the *bona fide* transferee takes a good title to the stock. The latter is not affected or bound to take notice of a *lis pendens* in that suit.

§ 362. *Lis pendens as affecting a purchase of stock.*—A purchaser of certificates of stock is not chargeable with constructive notice that a suit is pending, in which his vendor is defendant and the plaintiff is endeavoring to obtain possession and title to the stock which the purchaser is buying. The doctrine of *lis pendens* has no application to sales of shares of stock. The purchaser is bound to know that a judgment or decree has been rendered and executed, affecting the certificates he is buying, if such a judgment or decree exists, but he is not bound to know that a suit is pending, in which judgment has not yet been rendered. That a *lis pendens* in a suit involving shares of stock does not affect a purchaser of the certificate representing those shares, the purchase being made while the suit is pending, was clearly established by the Court of Appeals of New York, in the case of *Holbrook v. New Jersey Zinc Company*.³

C.—FORGERY.

§ 363. *Forgery as affecting a sale of stock.*—An owner of shares of stock cannot be deprived of his property by a forgery

57 N. Y. 616 (1874); *Leitch v. Wells*, 48 N. Y. 585 (1872).

¹ *Quarl v. Abbett*, 13 Am. & Eng. Corp. Cases, 27 (Ind. 1886).

² *Sprague v. Cacheco Mfg. Co.*, 10 Blatchf. 173 (1872).

³ 57 N. Y. 616 (1874), following *Leitch v. Wells*, 48 N. Y. 586 (1872). See *Dovey's*

Appeal, 97 Penn. St. 153 (1881), where the court refused to pass upon this question; also *Bank of Va. v. Craig*, 6 Leigh (Va.), 399, 435 (1885), holding that a *lis pendens* in a suit by sureties, to restrain guardian from selling stock, is not notice to the corporation to refuse to allow him to register a transfer.

through which his certificates of stock pass into the hands of innocent purchasers. He may be deprived of his stock, but has in lieu thereof the right to collect the value of that stock, either from the corporation or from parties who have held the stock. The rights and remedies of the stockholder, who has lost possession of certificates of stock by forgery, vary according to the extent to which his certificate has been transferred. This remedy may be against the transferees of the certificate before a registry has been obtained, or it may be against the corporation for allowing a registry, or it may be against the person obtaining the registry. The forgery itself may consist of any writing on the certificate of stock, whereby, with intent to defraud, it is falsely and materially so made or altered as to have an apparent legality.¹ Generally the forgery is of the name of the stockholder to the transfer or power of attorney on the back of the certificate.² The forgery may, however, be committed by changing the number of shares of stock which the transferrer has written out in the certificate,³ or by inserting the numbers of shares of stock of one corporation, in a blank transfer duly signed by the stockholder, but signed for the purpose of transferring shares of stock in another and different corporation.⁴ The forgery may also be by an officer of the corporation who forges the necessary names of the corporate officers to the certificate, and puts it in circulation.⁵

¹ See Bouvier's Dictionary, vol. I, p. 679; 2 Bishop's Criminal Law, § 523.

² Nearly all of the cases in several following sections are cases of a forgery of the stockholder's name to a transfer or a power of attorney. Signing a transfer instead of a power of attorney is about the same thing. "The difference between the two modes is theoretical rather than practical." *Boston & Albany R. R. Co. v. Richardson*, 135 Mass. 473 (1883). It is forgery for one trustee to write in the names of the other trustees without authority, *Cottam v. Eastern Counties Ry. Co.*, 1 J. & H. 243 (1860); *Sloman v. Bk. of Eng.*, 14 Sim. 475 (1845), or for one partner to write in the name of the other partner, without authority, where the stock stood in their joint names. *Midland Ry. Co. v. Taylor*, 8 H. L. Cases, 751 (1862), aff'g *Taylor v. Midland Ry. Co.*, 29 L. J. (Ch.) 731 (1860).

³ *Matthews v. Mass. Nat. Bk.*, 1 Holmes, 396 (1874); *Sewall v. Boston*

Water Power Co., 86 Mass. 277 (1862), where the alteration was treated as a forgery, so far as legal rights were concerned, although the alteration was due to an innocent misunderstanding of a clerk.

⁴ *Swan v. North British Co.*, 7 H. & N. 603 (1862), practically overruling *Ex parte Swan*, 7 C. B. N. S. 400.

⁵ *Shaw v. Port Philip & C. Gold Min. Co.*, L. R. 13 Q. B. D. 103 (1885), where the corporation was held liable on a certificate signed and issued by the secretary of the corporation, but who had forged thereto the names of the other corporate officers whose signatures were necessary to the issue of a certificate of stock. *Cf. Duncan v. Luntley*, 2 McN. & G. 30 (1849). By statute in many of the States such forgeries are made a special criminal offense. *Regina v. Nash*, 2 Denison's Crim. C. 493 (1852); *New York Penal Code*, § 591. See also *Manhattan Beach Co. v. Harned*, 27 Fed. Rep. 484 (1886), where, however, the is-

§ 364. *Rights and liabilities of transferees of forged certificates of stock, there being no intervening registry on corporate books.*—The position of a transferee of a certificate of stock which is invalid by reason of forgery, depends largely on whether there has been an intervening registry of transfer on the corporate books, since the former owner was deprived of his stock by the forgery. The forger himself is of course liable, not only to the real stockholder, but also to any other person who has been injured by the forgery. If the purchaser of stock, from one who has forged a transfer of the same, sells the same after being notified by the real owner, that the latter claims the stock and has been deprived of it by forgery, the real owner may recover damages in trover for the value of the stock from the person who so sells, although he purchased in good faith and without notice of the forgery.¹ If the forgery is committed by a member of a firm, the real owner may sue the firm for money had and received and may recover the value of the stock and dividends.² Where the forger has sold the stock to a purchaser without notice, and the latter has sold to another purchaser without notice, and the latter is deprived of his apparent ownership on account of the forgery, the second transferee may hold the first transferee liable.³ This principle grows out of the well established rule of law that, in a sale of chattels, there is an implied warranty of title, unless the circumstances are such as to give rise to a contrary presumption. The broker or auctioneer of stock which passes through their hands, cannot, it seems, be held liable, though it turns out that on account of a forgery, there was no title to the stock in the party whom they represented.⁴ The transferee, whose title to the stock he has purchased is based on a forgery, has no rights as against the corporation, where there has been no registry on the corporate books between the date of the forger's transfer and the date of the transfer first mentioned. He cannot compel the corporation to allow him to register his

sue was by fraud, rather than forgery. *Moore v. Citizens' Nat. Bk.*, 111 U. S. 157 (1883). See also § 294.

¹ *Monk v. Graham*, 8 Mod. 9 (1721).

² *Marsh v. Keating*, 1 Bing. New Cases, 198 (1834); *Marsh v. Stone*, 6 B. & C. 551 (1827).

³ *Matthews v. Mass. Nat. Bank*, 1 Holmes 396 (1874). This was an ex-

tremely harsh case, involving a rigid application of the principle, since the defendant's name appeared on the back of the certificate of stock as a transferrer, when in fact he had only been a pledgee, and on payment of the pledge had retransferred the stock.

⁴ *Machinists' Nat. Bk. v. Field*, 126 Mass. 345 (1879).

transfer. If the corporation has already registered him as transferee it may repudiate its registry, so far as *he* is concerned, and refuse to recognize him as a stockholder or as having the right to transfer the stock.¹ Such a registered transferee has no right of action against the corporation by reason of its rescission of his registry,² although the rule may be different if he purchased by reason of the fact that he was allowed such registry on the corporate books.³ On the other hand it is the transferee obtaining registry, who warrants the validity of his title and right to transfer, and if the corporation is compelled to pay damages to the real owner, on account of allowing such registry, it may have recourse to and collect the same damages from the transferee who obtained the registry, however innocent the latter may have been.⁴ The person who first obtains a registry after a forgery has deprived the real owner of his stock, cannot retain the new certificates as against the real owner of the old ones.⁵

§ 365. *Liability of corporation to real owner of stock for allowing registry of forged transfer.*—It is the duty of a corporation to prevent and refuse a registry of transfer of stock, where that transfer has been forged. If the corporation fails to detect the forgery it is liable to the real owner of the stock who has been deprived of it by the forgery.⁶ It has been held that

¹ *Simon v. Anglo-Am. Tel. Co.*, L. R. 5 Q. B. D. 188 (1879); *Whitewright v. American Tel. & Cable Co.*, N. Y. Daily Reg. Aug. 6th, 1886 (Superior Ct.); *Waterhouse v. London & S. W. Ry. Co.* 41 L. T. N. S. 553 (1880); *Hambleton v. Central O. R. R. Co.*, 44 Md. 551 (1876); *Brown v. Howard Ins. Co.*, 42 Md. 384 (1875); *Hildyard v. South Sea Co.*, 2 P. Wms. 76 (1722). Cf. *Ashby v. Blackwell*, 2 Eden, 299 (1765), holding the corporation liable not only to the real owner, but also to the transferee obtaining registry. See following section for rights of transferee of the first registered holder.

² *Id.*

³ *Metropolitan Sav. Bk. v. Mayor, &c. of Baltimore*, 63 Md. 6 (1884). In this case the plaintiff took the forged certificates in pledge from the forger. Afterwards, upon the forger's applying for a further loan on the same pledge of stock, corporation refused unless the stock was registered in its name, which was accordingly done. Held that the bank

lost the first loan, but had recourse to the corporation for the second loan.

⁴ *Boston & Albany R. R. Co. v. Richardson*, 135 Mass. 423 (1883), the court saying also in a *dictum*, that the defendant has a remedy over against the parties that sold to him.

⁵ *Johnston v. Renton*, L. R. 9 Eq. Cas. 181

⁶ *Pratt v. Taunton Copper Mfg. Co.*, 123 Mass. 110 (1877); *Sewall v. Boston Water Power Co.*, 86 Mass. 277 (1862); *Pratt v. Boston & Albany R. R. Co.*, 126 Mass. 443 (1879); *Johnson v. Renton*, L. R., 9 Eq. 181 (1870); *Cottam v. Eastern Counties Ry. Co.*, 1 J. & H. 243 (1860); *Midland Ry. Co. v. Taylor*, 8 H. L. Cases, 751 (1862); aff'g *Taylor v. Midland Ry. Co.*, 29 L. J. (Ch.) 731 (1860); *Davis v. Bk. of Eng.*, 2 Bing. 393 (1824); *Swan v. North British Aus. Co.*, 7 H. & N. 603 (1862), substantially overruling same case in court of law. *Ex parte Swan*, 7 C. B. N. S. 400 (1859); *Pollock v. National Bank*, 7 N. Y. 274 (1852); *Day v. American Tel. & Cable Co.*, N. Y. Daily

the owner of the stock may compel the corporation to cancel the illegal registry and restore the name of the plaintiff.¹ The better rule, however, is that, inasmuch as a *bona fide* transferee of the illegally registered transferer is entitled to retain the stock, the former owner of the stock in suing the corporation should demand relief in the alternative, that the stock be restored to him or that he be given damages in lieu thereof.² Or he may demand that the corporation replace the stock by going into the market, if necessary, and purchasing similar stock.³ If the stockholder sues the corporation for a dividend on stock which by a forged assignment has been registered in the name of another person, the corporation cannot interplead.⁴ A court of equity has concurrent jurisdiction with law in remedying a forged transfer of stock.⁵ The corporation, the co-conspirators and the transferees of the forged certificate are all proper parties to the suit,⁶ but the only necessary party is the corporation itself.⁷ Where the corporation is sued by the real owner of the stock for allowing the registry of a transfer based on forgery, it cannot institute an independent action bringing in all the parties interested and enjoining the action of the owner of the stock.⁸ The latter is entitled to his

Reg., July 18th (1885); *Dalton v. Midland Ry. Co.*, 12 C. B. 458 (1852); *Mayor, &c., of Baltimore v. Ketchum*, 57 Md. 23 (1881); *Coates v. London & S. W. Ry. Co.*, 41 L. T. N. S. 553 (1880); *Blaisdell v. Bohr*, 68 Ga. 56 (1881); *Sloman v. Bk. of Eng.*, 14 Sim. 475 (1845); *Telegraph Co. v. Davenport*, 97 U. S. 369 (1878), where the court says, "Upon the facts stated there ought to be no question as to the right of the plaintiffs to have their shares replaced on the books of the company and proper certificates issued to them, and to recover the dividends accrued on the shares after the unauthorized transfer; or to have alternative judgments for the value of the shares and the dividends. Forgery can confer no power nor transfer any rights. The officers of the company are the custodians of its stock books and it is their duty to see that all transfers of shares are properly made, either by the stockholders themselves or persons having authority from them. If upon the presentation of a certificate for transfer they are at all doubtful of the identity of the party offering it, with its owner, or if not satisfied of the genuineness of a power of attorney pro-

duced, they can require the identity of the party in the one case, and the genuineness of the document in the other, to be satisfactorily established before allowing the transfer to be made. In either case they must act upon their own responsibility. . . . Neither the absence of blame on the part of the officers of the company in allowing an unauthorized transfer of stock, nor the good faith of the purchaser of stolen property, will avail as an answer to the demand of the true owner."

¹ *Johnston v. Renton*, *supra*; *Cottam v. Eastern Counties Ry. Co.*, *supra*; *Sloman v. Bk. of Eng.*, *infra*.

² This is the usual prayer for relief in this country.

³ *Pratt v. Boston & Albany R. R. Co.*, 126 Mass. 443 (1879).

⁴ *Dalton v. Midland R. R. Co.*, 12 C. B. 458 (1852).

⁵ *Blaisdell v. Bohr*, 68 Ga. 56 (1881).

⁶ *Id.*

⁷ *Mayor, &c., of Baltimore v. Ketchum*, 57 Md. 23 (1881); *Pratt v. Boston & Albany R. R. Co.*, 126 Mass. 443 (1879).

⁸ *American Tel. & Cable Co. v. Day*, 52 N. Y. Superior Ct. 128 (1885).

action at law without delay and without involving or settling the respective rights of others.

§ 366. The right of the rightful owner of the stock to complain of the forgery, whereby his certificate has passed into the possession of another, may be barred by estoppel or ratification. Formerly it was held that the negligence of the owner of the stock would be a bar to his remedy.¹ Later decisions, however, have firmly established the rule, that "there must be either something that amounts to an estoppel, or something that amounts to a ratification in order to make the negligence a good answer."² Accordingly the rightful owner of the stock is held not to be barred of his remedy by the fact that the stockholder, a corporation, allowed its corporate seal to be in the possession of its secretary, whereby he sold the stock owned by the corporation;³ or by the fact that the owner delayed several months, during which time the forger escaped;⁴ or that he transferred on the back of the certificate only part of the shares specified in the certificate;⁵ or that he gave his address wrong, and thereby a letter of inquiry did not reach him;⁶ or that he allowed his clerk, the forger, to have access to his papers, and gave him blank transfers duly signed to use in transferring other stock;⁷ or that the guardian of the plaintiff was negligent.⁸

§ 367. *Rights of transferees who purchase after a registry has been obtained.*—It has already been shown that the transferees of a certificate of stock which has been put in circulation by forgery, are not allowed to retain such stock where there has not been, at some time subsequent to the forgery, a transfer registered on the corporate books. It has also been shown that he who applies to the corporation for a registry of transfer, such registry being the first one since the forgery was committed, is not allowed to retain the stock. An entirely different rule pre-

¹ *Coles v. Bk. of Eng.*, 10 Ad. & E. 437 (1839), where the continuous receipt of dividends on a less quantity of stock than she was entitled to, was held a bar, though the stockholder was old and infirm.

² *Bank of Ireland v. Trustees of Evans Charities*, 5 H. L. Cases, 389 (1855).

³ *Id.*

⁴ *Davis v. Bk. of Eng.*, 2 Bing. 393 (1824).

⁵ *Sewall v. Boston Water Power Co.*, 86 Mass. 277 (1862).

⁶ *Johnston v. Renton*, L. R. 9 Eq. 181 (1870).

⁷ *Swan v. North British Aus. Co.*, 7 H. & N. 603 (1862); substantially overruling *Ex parte Swan*, 7 C. B. (N. S.) 400 (1859).

⁸ *Telegraph Co. v. Davenport*, 97 U. S. 369 (1878).

vails as regards all subsequent *bona fide* holders of the new certificate obtained by the first registry. The person who obtains the first registry has no rights except as against his transferrer. But all subsequent purchasers without notice are fully protected. They cannot be compelled to give up the stock, either to the corporation or to the person who lost it by forgery.¹ This rule arises, not from the law of negligence, but from the law of estoppel operating against the corporation. It is in accord with the demands of trade, and the constant tendency of the law to protect *bona fide* purchasers of certificates of stock.

D.—STOLEN OR LOST CERTIFICATES.

§ 368. *Stolen or lost certificates of stock indorsed in blank as affecting the sale thereof.*—One of the most important elements of the negotiability of promissory notes is that if the holder of such note loses it, or it is stolen from him when it is indorsed in blank, a subsequent *bona fide* purchaser of such note is protected as against the person who lost it. A different rule seems to prevail as regards certificates of stock, indorsed in blank, and then lost or stolen. In this respect certificates of stock are not negotiable. It has been clearly held that a purchaser from a thief of certificates of stock indorsed in blank, is not protected, nor is any subsequent purchaser of *that identical* certificate allowed to claim the stock. The real owner of the certificate may compel the corporation, which has refused to recognize the thief's transferee's title, to register the stock as his, or he may have damages against a *bona fide* transferee of the thief, where such transferee sold with notice.² In Nevada it is

¹ *Machinists Natl. Bank v. Field*, 126 Mass. 345 (1879). *Re Bahia & San Francisco Ry. Co., L. R.*, 3 Q. B. 584 (1868), where, however, the corporation having cancelled all the registries made subsequent to the forgery, it was held liable in damages to a purchaser subsequent to the first registry. The court said, the giving of a certificate "is a declaration by the company to all the world that the person in whose name the certificate is made out and to whom it is given, is a shareholder in the company, and it is given by the company with the intention that it shall be so used by the person to whom it is given, and

acted upon in the sale and transfers of shares."

² *Barstow v. Savage Min. Co.*, 64 Cal. 388 (1883), substantially overruling *Winter v. Belmont Min. Co.*, 53 Cal. 428 (1879); *Anderson v. Nicholas*, 28 N. Y. 600 (1864), where the purchaser of the stolen certificate was not a *bona fide* purchaser. The court said that even if he had been a *bona fide* purchaser he would not be protected. *Cf. Aull v. Colket*, 33 Leg. Intel. 44 (1876, Penn.), where the question of negligence was submitted to the jury. The mere fact of losing it is no proof of negligence. *Biddle v. Bayard*, 13 Penn. St. 150 (1850).

held that the purchaser and vendor of the stolen certificate is liable in damages to its real owner, although the former acted as a broker and without notice.¹ The *bona fide* purchaser of a stolen certificate of stock indorsed in blank, cannot compel the corporation to register him as a stockholder.² The person stealing certificates of stock is guilty of larceny and may be convicted for the same.³ The corporation cannot obtain an injunction against a possible action by the purchaser of stolen certificates, who has applied for registry and been refused it.⁴

§ 369. Where, however, certificates of stock indorsed in blank have been stolen, and the thief or his transferee has obtained a registry on the corporate books, and obtained new certificates of stock, and these new certificates have been sold, the purchaser is protected in his possession of the stock.⁵ In Michigan this is held to be the rule, even though such purchaser took the stock with full knowledge of all the facts.⁶ It is to be hoped that this rule will be generally sustained, since it is in accordance with the general rule that the rights and equities of all holders of stock back of the registry and issue of the certificates in existence, are not allowed to affect the stockholdership or rights of purchasers of these new certificates.

§ 370. *Owner of a lost certificate of stock may obtain new certificate.*—An owner of a certificate of stock who has lost it or had it stolen from him may, by taking proper proceedings or by giving proper security to the corporation, have new certificates issued to him. In Louisiana it is held that upon satisfactory proof of the loss of certificates of stock, a writ of *mandamus* will issue to compel the corporation to issue new certificates, and that no bond of indemnity need be given.⁷ But the better rule seems to be that, except in cases of the clearest proof of loss, the corporation shall not be required to issue new certificates, unless a bond of indemnity against its liability to possible legal holders of the lost certificate shall be given.⁸ In New York, by statute,

¹ *Bercich v. Marye*, 9 Nev. 312 (1874).

² *Sherwood v. Meadow Valley M. Co.*, 50 Cal. 412 (1875).

³ *People v. Griffin*, 38 How. Pr. 475 (1869).

⁴ *Buffalo Grape Sugar Co. v. Alberger*, 22 Hun, 349 (1880).

⁵ *Mandlebaum v. North Am. Min. Co.*, 4 Mich. 465 (1857).

⁶ *Id.*

⁷ *State v. New Orleans Gas Light Co.*, 25 La. Ann. 413 (1873).

⁸ *Galveston City Co. v. Sibley*, 56 Texas, 269 (1882), where one who became a stockholder in 1841, died in 1865, and his heirs applied for a new certificate in 1878. The court said: "This indemnity should be governed by the circum-

security may be required in all such cases.¹ It would seem reasonable that a bond of indemnity should be given to the corporation, since in case the old certificate has not been lost, but has been sold by its owner, the corporation is liable in damages or to replace the stock to the purchaser, for issuing new certificates without a surrender of the old.²

E.—CONFISCATION OF STOCK.

§ 371. During the late Rebellion acts of confiscation were passed, both by the United States Government and by the Confederate Government, and shares of stock owned by parties in one section of the country, in corporations domiciled in the other section, were confiscated. The result of the war having established that the Confederate Government was an illegal one, all its acts of confiscation became null and void, and all transfers and registries of stock thereunder were held to be void utterly. The whole line of transactions based on the confiscation fell with the confiscation itself.³ The corporation was held not liable to purchasers whose title was based on the confiscation, since it acted under compulsion of a power temporarily greater than the law itself.⁴ If the corporation neglects to remedy the confusion and claims, growing out of the illegal confiscation of stock, any stockholder may institute an action in its behalf for that purpose.⁵ The stock is to be restored to the owner against whom the confiscation proceedings were had, and if the corporation, during the Rebellion, voluntarily paid divi-

stances of the particular case. If not only the loss, but also the destruction of the instrument and the ownership of the plaintiffs, should be clearly shown, then, if required at all, it would, as a general rule, be but nominal. . . . In view of the fluctuating value of this stock; the uncertainty when the necessity may arise for such bond of indemnity; the length of time it may run, and probable change in the solvency of the sureties; the continuing character of the relief which may be required from time to time; and the number and non-residence of the plaintiffs,—it is deemed proper in this case to adopt the practice, somewhat novel with us, but analogous to the proceedings of courts of chancery elsewhere, to require

that this case remain open on the docket below until from lapse of time or otherwise the rights of the parties shall be so established, that the case may be finally dismissed without prejudice to either party." *Societe Generale de Paris v. Walker*, L. R., 11 App. Cas. (H. of L.) 20; *aff'd* L. R., 14 Q. B. D. 424; *Butler v. Glen Cove Starch Co.*, 25 Hun, 47 (1879).

¹ N. Y. Session Laws, 1873, ch. 151.

² See §§ 358-360.

³ *Dewing v. Perdicaris*, 96 U. S. 193 (1877).

⁴ *Id.*, also *Central R. R. & Banking Co. v. Ward*, 37 Ga. 515 (1868).

⁵ *Perdicaris v. Charleston Gas Light Co.*, Chase's Dec. 435 (1869); *aff'd*, *sub nom. Dewing v. Perdicaris*, *supra*.

dends to the illegal holders of the stock, it must pay the same to the plaintiff, even though it would have been compelled to pay such dividends to the southern holder, if it had not done so voluntarily.¹ On the other hand, proceedings for the confiscation of stock under the confiscation acts of the United States Government, passed by reason of the late Rebellion, are held to have been effective, if in accordance with established rules of procedure. Where, however, no notice of the proceedings was given to the defendant, and her name and the stock were not accurately described, the proceedings were void, and the corporation, having obeyed the illegal judgment of confiscation, was held liable in damages to the southern owner of the stock.²

¹ *Keppel's Adm. v. Petersburg R. R. Co.*, Chase's Dec. 167 (1868). 85 N. Y. 437 (1881), reversing s. c. 12 J. & S. 340; *Avil v. Alexander Water*

² *Chapman v. Phoenix National Bank, Co.*, 1 Hughes, 408 (1877).

CHAPTER XXII.

SALES OF STOCK.—FORMAL METHOD OF TRANSFERRING CERTIFICATES, AND REGISTRY THEREOF.

§ 372. Subject treated herein.

373. The two usual steps in perfecting a transfer of stock.

374. Omission of either or both steps.

A.—METHOD OF TRANSFERRING THE CERTIFICATE.

§ 375. Usual forms of assignment and powers of attorney whereby the transferor assigns the certificate of stock to his transferee.

376. Questions which arise herein.

377. A seal is not necessary to a transfer of stock.

378. The assignment of the certificate of stock estops the transferor from claiming any further title in the stock, as against subsequent *bona fide* transferees, although such assignment be not registered.

379. Effect of charter provision requiring registry.

380. Certificate of stock may be assigned with the name of the transferee left blank.

B.—METHOD OF REGISTERING A TRANSFER OF STOCK.

§ 381. Registry an essential part of a transfer of stock.

§ 382. Formalities of making registry.

383. Formalities of registry may be waived by the corporation.

384. Either the transferor or the transferee may apply to the corporation for a registry of transfer.

C.—RIGHTS AND DUTIES OF THE CORPORATION IN ALLOWING OR REFUSING REGISTRY.

§ 385. Corporation may require proof of identity, also of genuineness of signature, &c.

386. Corporation cannot refuse registry on account of the motive of the transferor or transferee in the transaction.

387. Corporation may interplead between two claimants to stock.

388. Corporation must obey mandate of court ordering registry and issue of new certificates.

389. Remedies of a transferee of stock against the corporation for refusal to allow registry.

390. Remedy by mandamus.

391. Remedy by suit in equity.

392. Remedy by an action for damages.

§ 372. *Subject treated herein.*—Having considered the competency of parties to enter into a contract of sale of stock;¹ also of the legality, enforceability, and character of that contract;² also the rights of third parties as effecting the contract between the transferor and transferee;³ it is now necessary to discuss certain formalities of transfer connected with a sale of stock. These formalities are peculiar to sales of stock. The only analogy to them is, perhaps, that arising from the making of a deed of real estate, and a registry of the same at a recorder's office. In many respects,

¹ Ch. XIX.

² Ch. XX.

³ Ch. XXI.

however, this analogy does not apply. Thus the corporation itself has many rights and duties herein which a register of deeds has not. The principles of law governing the formalities of transfer of stock have occasioned great difficulties and much litigation. The rules given herein have arisen for the most part out of the necessities and demands of business as sanctioned by the courts. They have been gradually formed and still bear the imprints of the transition stage of a newly created law.

§ 373. *The two usual steps in perfecting a transfer of stock.*—To transfer a share of stock there generally are two distinct steps to be taken: first, the certificate is assigned by the transferrer to the transferee; and, second, that assignment and transfer is perfected and completed by delivering the assigned certificate to the corporation, obtaining an entry on the corporate transfer book to the effect that the transferee has purchased the stock of the transferrer, and taken from the corporation new certificates of stock certifying that the newly recorded stockholder owns a specified amount of stock.

§ 374. *Omission of either or both steps.*—Either and probably both of these two steps in the complete transfer of stock may be omitted, and yet, where the facts estop the various parties from denying that a transfer has been made, it will be held to be complete. That an owner of stock may transfer his stock to another without assigning a certificate to him has been frequently held.¹ This happens when a registry of transfer is made without any surrender of the old certificate.² So far as the transferrer is concerned such a method of transfer is effectual. Such cases also arise where the corporation has never issued certificates of stock. The stockholder may then transfer his stock without assigning a certificate.³

A.—METHOD OF TRANSFERRING THE CERTIFICATE

§ 375. *Usual forms of assignment and powers of attorney whereby the transferrer assigns the certificate of stock to his transferee.*—A certificate of stock is a paper issued by the corporation to a stockholder, stating that the person specified therein is

¹ See § 308; also Ch. XXVI.

² See §§ 358–360.

³ First Nat'l Bank v. Gifford, 47 Iowa,

575 (1877); *Brigham v. Mead*, 92 Mass. 245 (1865). See also § 382.

the owner of a certain number of shares of its capital stock.¹ The assignment of this certificate is made, it seems, in three different ways: first, it has been held that it may be made by a simple delivery of the certificate without any writing.² Again it may be made by a formal instrument of transfer duly signed by the transferrer. This instrument may be separate from the certificate of stock, but generally is printed in blank on the back of it.³ In either case, in order to make the transfer complete by a registry of it on the corporate books, it is necessary for the transferrer to go to the office of the corporation and sign the stub of its transfer book, whereby the transfer is recorded. The third and most usual method of assigning a certificate of stock is by a formal instrument of transfer, similar to the one explained above,⁴ united with a power of attorney authorizing a person, whose name is generally left blank, to be subsequently filled in, to sign the corporate registry book, whereby the transfer is recorded. This instrument of transfer and the power of attorney are generally printed in blank on the back of the certificate of stock.⁵ It

¹ The following form is quite usual:

The Toledo,
Ann Arbor, and North Michigan
Railway Company.

This certifies that _____ is entitled to _____ shares of the capital stock of the Toledo, Ann Arbor, and North Michigan Railway Company, transferable on the books of the company, in person or by attorney, on the surrender of this certificate. Toledo, _____, 1886.

JAMES M. ASHLEY, President.

H. W. ASHLEY, Secretary.

The word "only" is often inserted after "transferable."

² See § 308, where a delivery of a certificate of stock *causa mortis*, was held good, without any writing assigning the certificate. In *Fraser v. Charleston*, 11 S. C. 486 (1878), the court said in a *dictum*: "The court is impressed with the force of the proposition that the hypothecation of such securities by the legal owner, or by another person with the previous consent or subsequent acquiescence of the legal owner, without indorsement or power of attorney, may constitute by delivery an equitable assignment, and act as an estoppel against the legal owner and creditors claiming through him." *Cf. Sitgreaves v. Far-*

mers, &c. Bk., 49 Penn. St. 359; *Davis v. Bank of Eng.* 2 Bing. 393; *Burrall v. Bushwick R. R. Co.*, 75 N. Y. 211; *Dunn v. Com. Bk. of Buffalo*, 11 Barb. 580. See also Ch. XXVI.

³ A common form is:

For value received _____ hereby sell, assign, and transfer unto _____ all right, title, and interest in _____ shares in the capital stock of the Toledo, Ann Arbor, and North Michigan Railway Company. New York, _____, 18—.

In presence of: _____

Or if printed on the back of the certificate:

For value received _____ hereby sell, assign, and transfer unto _____ shares of the capital stock represented by the within certificate.

New York, _____, 18—.

In presence of: _____

⁴ *Id.*

⁵ A short form is:

For value received _____ hereby sell, assign and transfer unto _____ shares of the capital stock represented by the within certificates, and do hereby irrevocably constitute and appoint _____, attorney,

enables the transferee to obtain a registry without the presence of the transferrer, provided the corporate registry agent is satisfied with the signature and intent of the transferrer to assign the stock. This power of attorney is not revoked by the death of the transferrer before it is used.¹

§ 376. *Questions which arise herein.*—The assignment of a certificate of stock by the transferrer to the transferee, considered apart from the actual registry of such assignment on the corporate books, involves the questions whether such an assignment should be under seal; whether, after the assignment, the transferrer can claim any rights of ownership as against the transferee, even though there be no registry of the transfer; and whether a transfer and power of attorney duly signed by the transferrer, but left in blank as to the names of the transferee and attorney, are legal, and may pass from hand to hand until some holder cares to fill up the blanks. These and incidental questions are discussed in the following sections.

§ 377. *A seal is not necessary to a transfer of stock.*—In America, an assignment or transfer of a certificate of stock need not be under seal.² Formerly it was the custom to have all such transfers made by deed, duly sealed. As the nature of stock and certificates of stock, however, come to be understood more clearly,

to transfer the said stock on the books of the within named company, with full power of substitution in the premises.

New York, ———, 18—.

In presence of:

A longer form is:

Know all men by these presents, that ———, for value received, have bargained, sold, assigned, and transferred, and by these presents do— bargain, sell, assign, and transfer unto ——— of ——— shares in the capital stock of the Toledo, Ann Arbor, and North Michigan Railway Company, standing in ——— name on the books of the said company, and transferable only at its office in the city of Toledo. And ——— do hereby constitute and appoint ——— true and lawful attorney irrevocable, for ——— and in ——— name and stead, to ———, use, to sell, assign, transfer, and set over all or any part of the said stock; and for that pur-

pose to make and execute all necessary acts of assignment and transfer, and one or more persons to substitute, with like full power; hereby ratifying and confirming all that ——— said attorney or ——— substitute, or substitutes, shall lawfully do by virtue hereof.

In witness hereof ——— hereunto set ——— hand and seal, the ——— day of ———, one thousand eight hundred and ———.

Sealed and delivered in the presence of:

¹ Fraser v. Charleston, 11 S. C. 486 (1878); Leavitt v. Fisher, 4 Duer (N. Y.), 1 (1854); United States v. Cutts, 1 Sumner, 133 (1832).

² Quiner v. Marblehead Social Ins. Co., 10 Mass. 476 (1813); Atkinson v. Atkinson, 8 Allen, 15 (1864). If, however, the by-laws require it, the transfer must be under seal. Bishop v. Globe Co., 135 Mass. 132 (1883).

it became a rule of law that a transfer of the certificate, like the transfer of choses in action, did not require a seal. Not even the presence of the seal gives the transfer the character of a sealed instrument. The seal is a superfluity, and is disregarded.¹

In England, on the other hand, transfers of railway stocks are generally required by charter to be under seal. This is held to give the instrument the character of a deed; and hence, in accordance with the ancient technical rule of law, that a deed must be filled out as to the grantee and other essential particulars before it is sealed in order to be valid, it has been held in England that a transfer of a certificate of stock, duly signed and sealed, but with the name of the transferee in blank, is void absolutely.² In English companies, however, where the charter does not require transfers to be sealed, the transfer may be by an ordinary instrument in writing, and the presence of a seal will be disregarded.³

§ 378. *The assignment of the certificate of stock estops the transferrer from claiming any further title in the stock, as against subsequent bona fide transferees, although such assignment be not registered.*⁴—There is no case which denies this prin-

¹ German Union B. Assn. v. Sendmeyer, 50 Penn. St. 67 (1865); Commercial Bk. v. Kortright, 22 Wend. 348 (1839); McNiel v. Tenth Natl. Bk., 46 N. Y. 325 (1871); Bridgeport Bk. v. N. Y. & N. H. R. R. Co., 30 Conn. 231, 274 (1861).

² Hibblewhite v. McMorine, 6 M. & W. 200 (1840), per Parke, B.; Taylor v. Great Indian P. Ry. Co., 4 De G. & J. 559 (1859); Societe Gen. v. Tramways Union Co., L. R. 14 Q. B. D. 424 (1884), where transfer was to be by deed; aff'd, L. R. 11 App. 20.

³ *Re Tees Bottle Co.*, 33 Law Times, N. S. 834 (1876); Walker v. Bartlett, 36 Eng. L. & Eq. 369 (1856); *Re BARNED'S Banking Co.*, L. R. 3 Ch. 105 (1867); *Ex parte Sargent*, L. R. 17 Eq. 273 (1873); *Ortigosa v. Brown*, 47 L. J. (Ch.) 168 (1878). The American cases incline to the opinion that, even though a seal were required, the sealed transfer would not be void because of the blanks left in it. *Bridgeport Bk. v. N. Y. & C. R. R. Co.*, *supra*; *Com. Bk. v. Kortright*, *supra*; *Matthews v. Mass. Natl. Bk.*, 1 Holmes, 396, 407 (1874); *McNiel v. Tenth Natl. Bk.*, *supra*.

⁴ *Scott v. Pequonnock Bk.* (U. S. C. Ct.), 15 Rep. 137 (1883); *Brown v. Smith*, 122 Mass. 589 (1877); *Fitchburg Sav. Bk. v. Torrey*, 134 Mass. 239 (1883); *Duke v. Cahawba Nav. Co.*, 10 Ala. 82 (1846); *Chouteau Spring Co. v. Harris*, 20 Mo. 382 (1855); *St. Louis P. Ins. Co. v. Goodfellow*, 9 Mo. 149 (1845); *Gilbert v. Manchester Iron Mfg. Co.*, 11 Wend. 627 (1834); *Sargent v. Essex Mfg. Co.*, 26 Mass. 202 (1829); *Nesmith v. Wash. Bk.*, 23 Mass. 324 (1829); *Sargent v. Franklin Ins. Co.*, 8 Pick. 90 (1829); *Conant v. Reed*, 1 O. St. 298 (1853); *Baltimore City P. Ry. Co. v. Sewall*, 35 Md. 238 (1871); *Bk. of America v. McNiel*, 10 Bush, 54 (1873); *United States v. Vaughan*, 3 Binn. (Penn.) 394 (1811); *Beckwith v. Burroughs*, 13 R. I. 294 (1882); *Farmers & M. Bk. v. Wasson*, 48 Iowa, 336 (1878); *Carroll v. Mullanphy Sav. Bk.*, 8 Mo. App. 249 (1880); *B'way Bk. v. McElrath*, 13 N. J. Eq. 24 (1860); *Smith v. Crescent City, &c., Co.*, 30 La. Ann. 1378 (1878); *People's Bk. v. Gridley*, 91 Ill. 457 (1879). Nor can the transferrer avoid the assignment before registry on the ground that no consideration passed.

ciple of law. On close examination of the cases which seem to militate against it, it will be found that the issue involved was whether the unregistered transferee was protected against third persons, who claimed title back of the transferrer. The transferer himself is not allowed to impeach his unregistered transferee's title. Even in Connecticut, where, at an early day, the court held that the registry was the originating act of the title of the transferee, the court was considering the rights of third persons, and not the rights of the transferrer himself.¹ That the transferer cannot question the completeness of his transfer of title is a rule binding not only on himself, but also upon his assigns in bankruptcy or insolvency.² The transferrer is estopped also from attacking the assignment of the certificate on the ground of informalities in the transfer.³

§ 379. *Effect of charter provision requiring registry.*—This rule prevails, even though the certificate or by-laws, or charter itself, declares that a transfer shall not be legal, or complete, or effectual until it is registered on the corporate books.⁴ As between

Hall v. U. S. Ins. Co., 5 Gill (Md.), 484 (1847); Cushman v. Thayer Mfg. Co., 76 N. Y. 365 (1879). Such an assignment satisfies a contract to sell stock. White v. Saulsbury, 33 Mo. 150 (1862); Merchants Natl. Bk. v. Richards, 6 Mo. App. 454 (1879). The fact that the corporation subsequently refuses to register the transfer does not prevent title passing, as between transferrer and transferee. Crawford v. Provincial Ins. Co., 8 Upper Can. C. P. 263 (1859).

¹ Northrop v. Newtown & B. T. Co., 3 Conn. 552 (1821); Fisher v. Essex Bk., 5 Gray, 373 (1855), the rights of attaching creditors being involved.

² *Ex parte* Dobson, 2 Mont. D. & D. 685 (1842); Dickinson v. Central Natl. Bk., 129 Mass. 279 (1880); Morris v. Cannon, 8 Jur. N. S. 653 (1862); Sibley v. Quinsigamond Natl. Bk., 133 Mass. 515 (1882).

³ Holyoke Bk. v. Goodman Paper Mfg. Co., 9 Cush. 576 (1852); Maguire's Case, 3 De G. & S. 31 (1849); Sheffield A. & M. Ry. Co. v. Woodcock, 7 M. & W. 574 (1841); Cheltenham & G. W. N. Ry. Co. v. Daniel, 2 Q. B. 281 (1841); Home Stock Ins. Co. v. Sherwood, 72 Mo. 461 (1880). The legal sufficiency of the instrument of transfer cannot be questioned by the

transferrer. Chew v. Bk. of Baltimore, 14 Md. 299 (1859).

⁴ Johnson v. Laffin, 103 U. S. 800, 804 (1880); aff'g 5 Dill. 65 (1878); Noyes v. Spaulding, 27 Vt. 420 (1855), where the court says: "That provision is similar to the statute in this State in relation to the transfer of real estate, under which it has uniformly been held that the title passes to the grantee, as between the parties to the conveyance, though the deed is unrecorded. . . . The object of having the transfer recorded on the books of the corporation is notice, and that is the only object. For that reason the transfer, though unrecorded, is good against the party and all those who have notice in fact of the transfer." United States v. Cutts, 1 Sumner, 133 (1832); First Natl. Bk. v. Gifford, 47 Iowa, 575 (1877). The same provision was involved in nearly all the cases cited in preceding sections. See also Johnson v. Underhill, 52 N. Y. 203 (1873); Bk. of Utica v. Smalley, 2 Cowen, 770 (1824); Baldwin v. Canfield, 26 Minn. 43 (1879), where the court says that charter "provisions of this kind are intended solely for the protection and benefit of the corporation; they do not incapacitate a shareholder from transferring his stock without any entry upon the corporation books."

the transferrer and transferee, the unregistered assignment is complete and effectual in contradiction of such declarations. The courts construe these provisions of the certificate, or by-laws, or charter, to be intended, not to affect the rights of the transferee as against the transferrer, but to affect the rights of the transferee as against attaching creditors of his transferrer and other third parties claiming an interest in the stock, and also to affect his right to claim dividends, the privilege of voting, and other rights of a stockholder.¹

§ 380. *Certificate of stock may be assigned, with the name of the transferee left blank.*—By a commercial usage, which has been repeatedly recognized as valid by the courts, certificates of stock may be assigned by a transfer duly signed by the transferrer, but with the name of the transferee left blank.² Generally the combined instrument of transfer and power of attorney on the back of the certificate is signed by the stockholder and delivered to the purchaser, with the names of the transferee and of the attorney left blank. Such a certificate of stock, transferred in blank, may be sold and passed from hand to hand, and each purchaser of it is entitled to the same rights against his transferrer, or previous transferrers; as he would have if the names of the successive holders appeared on the certificate itself. Any purchaser of the certificate, duly signed but transferred in blank, may fill up the blanks and insert his own name.³ He may fill in his own name

¹ Continental Natl. Bk. v. Eliot Natl. Bk., 7 Fed. Rep. 369 (1881); Merchants, &c., Bk. v. Richards, 6 Mo. App. 654 (1879); and cases cited *supra*.

² Walker v. Detroit Transit Ry. Co., 47 Mich. 338 (1882); Pennsylvania R. R. Co.'s Appeal, 86 Penn. St. 80 (1878); Cutting v. Damerel, 88 N. Y. 410 (1882); German Union B. Assn. v. Sendmeyer, 50 Penn. St. 67 (1865); *Ex parte* Sargent, L. R. 17 Eq. 273 (1873); Ortigosa v. Brown, 47 L. J. (Ch.) 168 (1878); *Re* Barned's Banking Co., L. R. 3 Ch. 105 (1867). *Cf.* Walker v. Bartlett, 36 Eng. L. & Eq. 369 (1856). "Even in the absence of such usage, a blank transfer on the back of the certificate, to which the holder has affixed his name, is a good assignment; and a party to whom it is delivered is authorized to fill it up by writing a transfer and power of attorney over the signature." *McNiel v. Tenth*

Natl. Bk., 45 N. Y. 325, 331 (1871). "There is no force in the suggestion that the power of attorney in the present case was incomplete, because there were blanks for the number of shares and for the name of the attorney. Any holder might fill up the blanks and constitute himself the attorney. These points are too well settled to need discussion." *Holbrook v. New Jersey Zinc Co.*, 57 N. Y. 616, 623 (1874). As to the English rule, where the charter requires transfers to be under seal, see § 377.

³ *Broadway Bk. v. McElrath*, 13 N. J. Eq. 24 (1860); *Matthews v. Mass. Natl. Bk.*, 1 Holmes, 396 (1874); *Bridgeport Bk. v. N. Y. & N. H. R. R. Co.*, 30 Conn. 231 (1861). In the case *Kortright v. Buffalo Com. Bk.*, 20 Wend. 91 (1838); *aff'd*, 22 Wend. 348 (1839), Judge Nelson said: "This blank was afterwards filled up by the plaintiff by writing over the

as transferee, and the name of an agent as the attorney to make the registry, or he may leave the latter blank and allow the registry clerk to fill in his own name, as is frequently done.

B.—METHOD OF REGISTERING A TRANSFER OF STOCK.

§ 381. *Registry an essential part of a transfer of stock.*—

The effect of obtaining a registry, or of neglecting to obtain a registry of the transfer, on the corporate books, immediately after purchasing the same from the vendor, has given rise to much litigation and much apparent confusion. A registry of the transfer is important in two respects: first, as regards the rights of the purchaser in reference to the corporation; second, in regard to the rights of the purchaser as regards third persons, who are either creditors of the old registered stockholders or have claims upon the stock in question. So far as the corporation is concerned, it is bound to recognize only the registered stockholders.¹ To him is accorded the right to vote, draw dividends, and exercise the general rights of stockholdership. The unregistered purchaser of stock cannot claim such rights. All the cases agree in this result of a neglect to register a transfer. As regards the rights of third persons, however, the courts of the different States vary widely in their opinions. Generally the question arises by reason of an attachment or execution levied by a creditor of the transferrer

signature the transfer directly to himself, and the power of attorney to Sherwood, all which is in strict conformity with the universal usage of dealers in the negotiation and transfer of stocks, according to the proof in the case. Even without the aid of this usage, there could be no great difficulty in upholding the assignment. . . . The filling up is but the execution of an authority clearly conveyed to the holder, is lawful in itself, and convenient to all parties, as it avoids the necessity of needlessly multiplying transfers upon the books." To same effect, *Otis Admr. v. Gardner*, 105 Ill. 436 (1883); *Mount Holly, L. & M. T. Co. v. Ferrie*, 17 N. J. Eq. 117 (1864); *Prall v. Tilt*, 28 N. J. Eq. 479 (1877). In the case, *Leavitt v. Fisher*, 4 Duer, 1, 20 (1854), the court said that the power of attorney "is not limited to the person to whom it may first have been delivered, but enures to the benefit of each *bona fide* holder into

whose hands the certificate and power may subsequently pass, each successive holder having the right to fill up the blanks and execute the power, or cause it to be executed, whenever the protection of his own interests, as a pledgee or absolute owner, may require it. That the power is not exhausted by the first use to which it is applied, nor revoked by the death of the party giving it, but, unless surrendered to the person who gave it, or cancelled, continues in force until its execution by an actual transfer of the shares to which it relates; and that the validity, neither of the power or of the transfer, is at all affected by the number of the persons through whose hands the certificate and power, since their first delivery, may have passed."

¹ Registry herein means not only an actual registry, but also a request to the corporation to allow registry, where improperly refused by it. See § 382.

against the stock standing on the corporate books in the name of the transferrer, who has already sold and assigned the certificate of stock to another. As a general rule, it may be said that a purchaser of a certificate of stock is usually protected as fully without a registry on the corporation books as he would be by a registry, so far as subsequent attachments and most other possible equities against the stock are concerned. This is the rule in New York and most of the States. In Connecticut, New Hampshire, Illinois, and a few other States, a contrary rule prevails. In Massachusetts, a late statute has changed the old Massachusetts rule, so that it now accords with that of New York.¹

§ 382. *Formalities of making registry.*—The customary method of registering a transfer of stock on the corporate books is simple. The registered stockholder, or his attorney in fact, whose name is written in the blank power of attorney, applies to the corporate officer having charge of the transfer books, and requests a registry of the transfer to a person designated by the stockholder, either personally or by a name written in the blank transfer. Books of transfer are kept for purposes of registering, and upon such an application and a surrender of the old certificate, the old stockholder or his attorney makes the registry, and a new certificate is issued.²

Any suitable registry or stock list, or formal entry on the corporate books suffices. No special book need be kept for that purpose.³ The demand for registry should be made upon the principal officer or clerk, at the office of the corporation. When

¹ This statute is given in full in the Chapter on Attachments and Executions.

² *Burrall v. Bushwick R. R. Co.*, 75 N. Y. 211 (1878), the court saying: "We know how, as a usual thing, a transfer of stock is made. It has been proven many times in the courts, and the process is recited in the reports. An assignment of the stock in writing, is made by the former owner of it, with a power of attorney to transfer it on the books of the corporation. Books of transfer are kept for that purpose, and on the production of those papers, the nominated attorney makes the formal transfer, the old certificate is canceled, and a new certificate is issued to the new owner." In the case *Green Mount & S. L. T. Co. v. Bulla*, 45 Ind. 1 (1873), the court says that the corporate officer, having charge of the regis-

try book, is the proper person to make the registry, unless the by-laws prescribe otherwise.

³ "All that is necessary, when the transfer is required by law to be made upon the books of the corporation, is that the fact should be appropriately recorded in some suitable registry or stock list, or otherwise formally entered upon its books. For this purpose the account in a stock ledger, showing the names of the stockholders, the number and amount of the shares belonging to each, and the sources of their title, whether by original subscription and payment, or by derivation from others, is quite suitable, and fully meets the requirements of the law." *National Bank v. Watsontown Bank*, 105 U. S. 217 (1881).

so made, it is sufficient.¹ The method of registry may be regulated by the by-laws of the corporation. Thus, a by-law that the stock shall be transferable by indorsement in writing, made in the presence of the cashier or two other witnesses, has been sustained as valid, and is complied with only by the presence and signature of the cashier or of the witnesses.² So also of a by-law requiring registry in the presence of the president and secretary of the company.³ But a by-law requiring the assent of the president of the corporation to the registry of a transfer, would be in restraint of trade and void.⁴ A delivery of certificates to the corporation, and a mere request to the corporate officers to make the transfer is not a registry, until the entry is actually made.⁵

The fact that the registry clerk marks on the instrument of transfer the words "received for record," does not constitute a registry.⁶ It has been held that where the corporation has a branch registry office in another State, a registry in the branch office is not an effectual registry, until it has been reported and entered in the books of the main office of the corporation.⁷ If the corporation does not keep books for the registry of transfers of stock, a mere notice to the corporation that a transfer has been made constitutes a registry.⁸ But if the statute or charter requires a transfer to be made on the corporate books, no registry is possible until such books are obtained and opened.⁹ If the

¹ "It is sufficient for him to apply at the bank during the usual hours of business, and make his demand upon the officers and clerks who may be in attendance there, and in case they are not authorized to transact that particular business, they must either refer him to the proper officer in the bank, or procure the attendance of such officer, or of the board of directors, if necessary, without any unreasonable delay. . . . In the absence of any proof to the contrary, it may be fairly presumed, that the principal officer or clerk in attendance at the bank, during the usual hours of business, is authorized to permit such a transfer when proper." *Com. Bank of Buffalo v. Kortright*, 22 Wend. 348, 351 (1839); *Case v. Bank*, 100 U. S. 446 (1879), where application to the cashier was held to be proper; *McMurrich v. Bond H. H. Co.*, 9 U. C. (Q. B.) 333 (1852), where the application was to the secretary; *Re Goodwin v. Ottawa & P. Ry. Co.*, 13 U. C. (O.

P.) 254 (1863), where an application to secretary and treasurer was sustained; *Green Mount. & S. L. T. Co. v. Bulla*, *supra*, where the application was to the president.

² *Dane v. Young*, 61 Me. 160 (1872).

³ *Planters and M. M. Ins. Co. v. Selma Sav. Bk.*, 63 Ala. 585 (1879).

⁴ *Sargent v. Franklin Ins. Co.*, 8 Pick. 90 (1829).

⁵ *Brown v. Adams*, 5 Biss. 181 (1870). Nor will a mere entry of credit to the transferee, on the treasurer's books, suffice. *Marlborough Mfg. Co. v. Smith*, 2 Conn. 579 (1818).

⁶ *Northrop v. Curtis*, 5 Conn. 246 (1824).

⁷ *Pinkerton v. Manchester & L. R. R. Co.*, 42 N. H. 424 (1861).

⁸ *Crawford v. Prov. Ins. Co.*, 8 U. C. (C. P.) 263 (1859).

⁹ *McCurry v. Suydam*, 10 N. J. Law, 245 (1828).

corporation never issues certificates of stock, the stockholder cannot demand them.¹ If the corporation cannot allow the registry, on account of an injunction, it is nevertheless bound to respect the rights of a transferee who gives notice to it of the transfer.² The issue of a new certificate of stock is not essential to the completeness of a registry of the transfer.³ If the corporation delays unreasonably in allowing a registry it is liable in damages to the applicant for registry.⁴

The instrument of transfer must be in a proper form.⁵ Unless the old stockholder, or his duly authorized attorney, offers to make the registry, the corporation may refuse to allow it.⁶ The power of attorney must run from the previous registered stockholder, and not from an intermediate unregistered transferee of the certificate.⁷ Transfers under bankruptcy or insolvent laws, are to be registered like voluntary transfers.⁸ In England, a written acceptance of the stock by the transferee is required.⁹

A mere notice to the corporation that an assignment has been made, need not be considered by the corporation.¹⁰ Where, however, the transferee giving such notice, does not obtain registry, because the corporation refuses, for any reason, to make the registry, the mere notice must be borne in mind by the corporation, and the rights of the applicant preserved by it, as regards future registries.¹¹

§ 383. *Formalities of registry may be waived by the corporation.*—The corporation may waive the formalities connected

¹ *Thorp v. Woodhull*, 1 Sandf. Ch. 411 (1844); see §§ 74, 192.

² *Purchase v. New York Exchange Bk.*, 3 Rob. 164 (1865).

³ *First Natl. Bk. v. Gifford*, 47 Iowa, 575 (1877); *Chouteau Spring Co. v. Harris*, 20 Mo. 382 (1855).

⁴ *Sutton v. Bank of Eng.*, 1 C. & P. 193 (1824), where the bank delayed longer than one day, the customary time, and refused to give any reason therefor. *Catchpole v. Ambergate, N. &c., Ry. Co.*, 1 El. & B. 111 (1852), where, by reason of the delay, the stock was forfeited, notice of forfeiture going to the old stockholder.

⁵ *Queen v. General Cemetery Co.*, 6 E. & B. 415, holding that the deed of transfer, where a deed is necessary, must be properly drawn. See also *Societe Generale, &c. v. Walker, L. R.*, 11 App. 20.

⁶ *Mechanics Banking Assn. v. Mariposa Co.*, 3 Rob. (N. Y.) 395 (1865).

⁷ *Dunn v. Com. Bk.* 11 Barb. 580 (1852).

⁸ *Dutton v. Connecticut Bank*, 13 Conn. 493 (1840); *State v. Ferris*, 42 Conn. 560 (1875).

⁹ *Ortigosa v. Brown*, 47 L. J. (Ch.) 168 (1878). The Joint-Stock Company's Act of 1856, required such an acceptance. The Act of 1862, repealing the Act of 1856, prescribed that transfers should be made as was customary, unless the by-laws prescribed otherwise. Hence, in the absence of by-laws, the written acceptance is held to be customary and necessary.

¹⁰ *Stockwell v. St. Louis M. Co.*, 9 Mo. App. 133 (1880).

¹¹ *Supra*, note 2. See also Chapter on Liens.

with a registry of transfer, and when it does so, the transferee becomes a stockholder as completely as though registry had been regularly made.¹ Frequently the waiver arises by placing the transferee's name on the list of stockholders, although no formal registry has been had.² Even a charter requirement, that the consent of the directors to a registry of transfer shall be obtained, may be waived by the corporation.³ The corporation, by paying dividends to an unregistered transferee of stock, thereby waives the formalities of registry.⁴ When the corporation refuses to allow a registry, for reasons other than those connected with the mere formalities of registry, or for reasons not given to the applicant, it waives its right to insist on them, and cannot afterwards claim that the applicant did not conform to such technicalities.⁵ A failure, however, on the part of the corporation to notify the transferee of a refusal to allow registry is no waiver of such registry.⁶

§ 384. *Either the transferrer or the transferee may apply to the corporation for a registry of transfer.*—A person who appears on the corporation books as the holder of stock, but who,

¹ *Richmondville Mfg. Co. v. Prall*, 9 Conn. 487 (1833); *Clowes v. Brettell*, 11 M. & W. 461 (1843); *Sadler's Case*, 3 De G. & S. 36 (1849); *Chambersburg Ins. Co. v. Smith*, 11 Penn. St. 120 (1849); *Walter's Case*, 3 De G. & S. 149 (1850); *Baine v. Whitehaven, &c., Ry. Co.*, 3 H. L. C. 1 (1850); *Wills v. Murray*, 4 Ex. 843 (1850); *Yelland's Case*, 5 De G. & Sm. 395 (1852); *Powers v. Harding*, 1 C. B. (N. S.) 533 (1857); *Henderson v. Royal British Bk.*, 26 L. J. (Q. B.) 112 (1857); *Daniell v. Id.*, 1 H. & N. 685 (1857); *East G. Ry. Co. v. Bartholomew*, L. R., 3 Ex. 15 (1867); *Ind's Case*, L. R., 7 Ch. 485 (1872); *Weber v. Fickey*, 52 Md. 500, 516 (1879); *Home Stock Ins. Co. v. Sherwood*, 72 Mo. 461 (1880); *Isham v. Buckingham*, 49 N. Y. 216 (1872), where the court says: "It has never been held that a corporation can avail itself of its own negligence as a basis of a cause of action against a stockholder, nor that it is competent to waive a performance of its own rules, nor that it may not be estopped by its own acts and official declarations, the same as natural persons. If it did not provide a transfer book, or did not transfer the stock according to the prescribed forms, the fault was its own, and not the

defendant's. It could waive the observance of any other rules which it had adopted."

² *Upham v. Burnham*, 3 Biss. 431, 520 (1873).

³ *Ex parte Walton*, 26 L. J. (Ch.) 545 (1857). Likewise where the by-laws contain such a provision. *Chambersburg Ins. Co. v. Smith*, 11 Penn. St. 120 (1849), holding also that an oversight whereby the attorney who makes the registry omits to sign the registry is immaterial.

⁴ *Cutting v. Damerel*, 88 N. Y. 410 (1882).

⁵ *Townsend v. McIver*, 2 S. C. 25 (1870); *Bond v. Mt. Hope Iron Co.*, 99 Mass. 505 (1868), holding that the corporation must put the refusal on the ground of non-conformity with formalities, at the time of the application, and cannot afterwards raise such. *Chouteau, &c., Co. v. Harris*, 20 Mo. 382 (1855); *Robinson v. Natl. Bk. of New Berne*, 95 N. Y. 637 (1884), where the court says: "The requirement of a registry, existing only for its own protection and convenience, must be deemed waived and non-essential when it wrongfully refuses to obey its own rule."

⁶ *Gustard's Case*, L. R., 8 Eq. 438 (1869).

in fact, has sold the stock, has a right to have his transfer recorded on the corporate books, thereby releasing him from liability on the stock.¹ The vendor may request the corporation to register the transfer, and the corporation may make it at his request. If it refuses so to do, the vendor may bring suit in a court of equity to compel the corporation to register the transfer.² It has been held, also, that an intermediate vendor, of the stock, whose name has never appeared on the corporate books, may likewise compel a registry to be made.³ After an ultimate vendee has been registered, the original vendor cannot have an intermediate vendee and vendor registered as the stockholder.⁴ The corporation may register the transfer, even against the wishes of the transferee.⁵ The transferee also has a right to apply for and compel a registry of the transfer of stock to himself.⁶

C.—RIGHTS AND DUTIES OF THE CORPORATION IN ALLOWING OR REFUSING REGISTRY.

§ 385. *Corporation may require proof of identity, also of genuineness of signature, &c.*—When a transfer of stock is presented to the corporation for registry, if the corporation is in doubt as to the identity of the person presenting it, whether he be the stockholder already registered on the books or the attorney of such, the corporation may require proof of such identity.⁷ If

¹ "The purchase was in itself authority to the vendor to make the transfer. . . A court of equity will compel a transferee of stock to record the transfer, and to pay all calls after the transfer. . . If so, it is clear that the vendor may himself request the transfer to be made." *Webster v. Upton*, 91 U. S. 65, 71 (1875). "If a subsequent transfer of the certificate be refused by the bank, it can be compelled at the instance of either of them." *Johnston v. Laffin*, 103 U. S. 800, 804 (1880).

² *Wynne v. Price*, 3 De G. & S. 310 (1849); *Birmingham v. Sheridan*, 33 Beav. 660; *Eustace v. Dublin, T. C. Ry. Co., L. R.*, 6 Eq. 182 (1868).

³ *Paine v. Hutchinson*, L. R., 3 Ch. 388 (1868).

⁴ *Shaw v. Fisher*, 5 De G., M. & G. 596 (1855).

⁵ *Upton v. Burnham*, 3 Biss. 520, 525 (1873).

⁶ *Norris v. Irish Land Co.*, 8 E. & B. 512 (1857); *Daly v. Thompson*, 10 M. & W. 309 (1842); *Johnston v. Laffin*, 5 Dill. 65 (1878); 103 U. S. 800; *Hill v. Pine River Bank*, 45 N. H. 300 (1864); *Presbyterian Con. v. Carlisle Bk.*, 5 Penn. St. 345 (1847); *Mechanics Bk. v. Seton*, 1 Peters, 299 (1828); *Arnold v. Suffolk Bk.*, 27 Barb. 424 (1857); *Sargent v. Franklin Ins. Co.*, 8 Pick. 90 (1829); *Cushman v. Thayer Mfg. Co.*, 76 N. Y. 365 (1879). But the complaint must be full and accurate in its averments. *Edwards v. Sonoma Bank*, 59 Cal. 136 (1881).

⁷ *Telegraph Co. v. Davenport*, 97 U. S. 369 (1878), the court saying: "The officers of the company are the custodians of its stock books, and it is their duty to see that all transfers of shares are properly made, either by the stockholders themselves, or persons having authority from them. If, upon the presentation of a cer-

it is in doubt as to the competency of the transferrer to sell the stock,¹ legal proof of such competency must be given.² If the applicant for registry applies as the attorney of the registered stockholder, the corporation may require satisfactory evidence of the genuineness of the latter's transfer, or may require the presence of the stockholder himself.³

§ 386. *Corporation cannot refuse registry on account of the motive of the transferrer or transferee in the transaction.*—The corporation has nothing to do with the motive or purpose of the vendor or vendee of the stock.⁴ It can refuse a registry only when there is doubt as to the legal right of the applicant to have such registry. It cannot refuse on the ground that the transfer would injure the corporation, nor on the theory that the object of the transfer was to increase the votes of the transferee.⁵

§ 387. *Corporation may interplead between two claimants to stock.*—The task imposed upon a corporation in determining whether to refuse or to allow a registry of stock is a difficult and dangerous one. It is easy to avoid the risk of forgery or of failure of the applicant to identify himself. But circumstances frequently are such that the corporation dare not allow registry to either of two parties, each of whom claims to be the sole and absolute owner of the stock, and each of whom claims the right of registry or notifies the corporation not to register the other claimant as a stockholder. These cases arise on various occasions, but most often where the stock has been attached or sold on execution by the transferrer's creditors, before the transferee has obtained registry; or where, by the fraud of the old stockholder's agent, the certificate has passed into the hands of a *bona fide* purchaser; or where, by a breach of trust, an executor or administrator, or trustee or guardian, has sold the trust stock and appropriated the

tificate for transfer, they are at all doubtful of the identity of the party offering it with its owner, or if not satisfied of the genuineness of a power of attorney produced, they can require the identity of the party in the one case, and the genuineness of the document in the other, to be satisfactorily established before allowing the transfer to be made." *Davis v. Bank of Eng.*, 2 Bing. 393 (1824), where the court says the corporation "may take reasonable time to make inquiries; and

require proof that the signature to a power of attorney is the writing of the person whose signature it purports to be." *Bayard v. Farmers & M. Bk.*, 52 Penn. St. 232 (1866).

¹ See §§ 318, 319.

² *Id.*

³ *Supra*, note 7, and see §§ 363-367.

⁴ *Townsend v. McIver*, 2 S. C. 25 (1870).

⁵ *Moffatt v. Farquhar*, L. R. 7 Ch. D. 591 (1878).

proceeds; or under other states of fact wherein there are two claimants of the stock, each having rights which can be clearly ascertained only by litigation. It is not incumbent on the corporation to decide between these conflicting parties and rights.¹ Such a requirement would expose it to unreasonable risks and compel it to assume the functions of a court. Where there is a reasonable doubt as to the facts involved or as to the respective rights of the claimants of the stock, and the corporation is sued by one of the claimants for refusing to allow a registry by him, the corporation may interplead and thus compel the claimants to ascertain their rights through the medium of a court of justice.² A similar interpleader may be made where the corporation is sued for dividends which are claimed by two opposing parties.³ An interpleader is proper, however, only when suit is actually commenced against the corporation.⁴ There is some doubt and considerable difficulty in laying down rules as to when a corporation may safely claim a right to refuse to act, and to compel the

¹ The discussion of these various difficulties and circumstances is made under chapters devoted to them. Suffice it here to say in general that when the corporation actually issues a certificate of stock to an applicant for registry, it assumes a liability thereby, sometimes to claimants of the old certificate, sometimes to the purchaser of the new, according to the facts of the case. As regards the latter the case of *Moores v. Citizens' Nat. Bk.*, 111 U. S. 156, 165 (1883), well says: "A certificate of stock in a corporation, under the corporate seal, and signed by the officers authorized to issue certificates, estops the corporation to deny its validity as against one who takes it for value, and with no knowledge or notice of any fact tending to show that it has been irregularly issued."

² *Mechanics' Bk. v. Richards*, 6 Mo. App. 454 (1881), aff'd 74 Mo. 77; *State Ins. Co. v. Gennett*, 2 Tenn. Ch. 100; *Leavitt v. Fisher*, 4 Duer (N. Y.), 1 (1854). If the court decides that the interpleader is properly filed by the corporation herein, it generally on a motion dismisses the proceeding with costs to the corporation, and the court also decides between the defendants, if the case is ready as between them. If not ready, it directs an action or an issue, or a reference to a master, to ascertain contested

facts, as may be best suited to the nature of the case, "or the court may leave it to the defendants to prepare the case between them as they may be advised, which would be the effect of a general order to interplead." *State Ins. Co. v. Gennett*, 2 Tenn. Ch. 100 (1874), citing as cases on above rules of practice, *East. & West. &c. Co. v. Litledale*, 7 Hare, 62; *Martinius v. Helmuth*, 2 V. & B. 412, note; *Horton v. Baptist Church*, 34 Vt. 317; *Rowe v. Hoagland*, 3 Hal. Ch. 139; *Crawford v. Fisher*, 1 Hare, 441; *Condit v. King*, 2 Beas. Ch. 383; *Hendrickson v. Decow*, Sax. 595; *City Bk. v. Bangs*, 2 Paige, 570; *Angell v. Hadden*, 16 Ves. 212. The case, *State Ins. Co. v. Gennett*, 2 Tenn. Ch. 82 (1874), says: "The law is that the mere pretext of a conflicting claim is not sufficient. The court must be able to see from the facts stated that there is a question to be tried."

³ *Salisbury Mills v. Townsend*, 109 Mass. 115 (1871). Quere as to whether an action for dividends can be maintained before the right of the claimant to the stock is established. *Hughes v. Vermont Copper Min. Co.*, 72 N. Y. 207 (1878).

⁴ *Buffalo Grape Sugar Co. v. Alberger*, 22 Hun, 349 (1880).

claimants to litigate between themselves, before it allows a registry to either. The policy of the law doubtless is to go very far in allowing the corporation to refuse to incur responsibility by taking action. Where, however, the rights of one claimant is reasonably clear, the corporation should suspend action for a reasonable time within which the contesting party may apply to the courts, and if no such action is brought, it should allow a registry by the first named claimant.¹ Any other rule would enable any person to practically deprive a stockholder of the possession of his stock temporarily, by simply notifying the corporation that he claims the stock.² Where, however, the corporation has allowed one claimant to register his transfer, the right of the corporation to interplead is gone.³ It cannot afterwards remove the name of the registered stockholder, especially where such stockholder has acted in reliance upon such registry.⁴

§ 388. *Corporation must obey mandate of court ordering registry and issue of new certificates.*—The authorities on this proposition of law are few in number, but they are decisive in protecting the corporations from liability where it proceeds under mandate of a court. Thus, where a decree is obtained commanding the corporation to register a transfer, the corporation is protected in obeying the decree, even though it is reversed on appeal, there having been no stay of proceedings.⁵ Cases herein may arise also, where the registered stockholder alleges that he has lost his certificate, and the court compels the corporation to issue to him a new one;⁶ also where an attachment or execution has been levied, the old certificate of stock being outstanding.⁷ There is a limit, however, to the power of courts in these matters. If the whole capital stock has been issued and the certificates therefore are outstanding, a court cannot order the issue of other

¹ *Townsend v. McIver*, 2 S. C. N. S. 25 (1870).

² *Re Tahiti Cotton Co.*, L. R. 17 Eq. 273 (1874); *Ex parte Sargent*, L. R. 17 Eq. 273 (1873).

³ *Dalton v. Midland Ry. Co.*, 12 C. B. 458 (1852); *Cady v. Potter*, 55 Barb. 463 (1869); *Mt. Holly, L. & M. T. Co. v. Ferrie*, 17 N. J. Eq. 117.

⁴ *Ward v. Southeastern Ry. Co.*, 6 Jur. N. S. 890 (1860); *Hart v. Frontino, & Co.*, 22 L. T. N. S. 30; *Cohen v. Gwynn*, 4 Md. Ch. 357 (1848). Unless

there clearly is a clerical mistake and the issue is to the wrong party. *Smith v. North Am. Min. Co.*, 1 Nev. 423 (1865). The corporation is liable for such mistakes. *Harrison v. Pryse, Bernardistan (Fol.) Ch.* 324 (1740).

⁵ *Chapman v. New Orleans, G. L. & Banking Co.*, 4 La. Ann. 153 (1849). See also *Purchase v. New York Exchange Bank*, 3 Rob. 164 (1865).

⁶ See §§ 368-370.

⁷ See Ch. on Attachment and Execution.

certificates, unless the decree at the same time practically nullifies a corresponding outstanding certificate.¹

§ 389. *Remedies of a transferee of stock against the corporation for refusal to allow registry.*—Where, for any reason, the corporation refuses to allow the registry of a transfer of stock, when it is the duty and obligation of the corporation to allow it, the transferrer or the transferee who applies for registry may, in general, pursue one of three remedies. He may apply to a court of law for a mandamus to the corporation to compel it to open its books and allow the registry; or he may bring a suit in equity, praying that the corporation be decreed to allow the registry, or to pay him damages, if registry is impossible; or he may sue the corporation at law for damages, on the ground that by its refusal it has been guilty of a conversion of his stock.

§ 390. *Remedy by mandamus.*—The authorities are in irreconcilable conflict on the question whether a mandamus lies to compel a corporation to allow a registry on its books of a transfer of stock. The weight of authority holds very clearly that the mandamus will not lie under such circumstances.² This rule is

¹ See § 284.

² The leading case in this country is *Shipley v. Mechanics Bank*, 10 Johns. 484 (1813), where the court says: "The applicants have an adequate remedy by a special action on the case, to recover the value of stock if the bank have unduly refused to transfer it. There is no need of the extraordinary remedy by mandamus in so ordinary a case. It might as well be required in every case where trover would lie. It is not a matter of public concern, as in the case of public records and documents; and there cannot be any necessity, or even a desire of possessing the identical shares in question." *Ex parte Firemen's Ins. Co.*, 6 Hill, 243 (1843); *People v. Parker Vein Coal Co.*, 10 How. Pr. 543 (1854); *State v. Rombauer*, 46 Mo. 155 (1870); *State v. St. Louis, &c. Co.*, 21 Mo. App. 526 (1886); *King v. London Assurance Co.*, 1 Dowl. & R. 510 (1822); *Stackpole v. Seymour*, 127 Mass. 104 (1879); *King v. Bank of Eng.* 2 Doug. 524; *State v. Guerrero*, 12 Nev. 105 (1877); *State v. Miller*, N. Y. Daily Reg. April 10, 1886; *Baker v. Marshall*, 15 Minn. 177 (1870), where the stock had already been issued to another;

Wilkinson v. Prov. Bk., 3 R. I. 22 (1853); *Kimball v. Union Water Co.*, 44 Cal. 173 (1872); *Birmingham Fire Ins. Co. v. Com.*, 92 Penn. St. 72 (1879), where the court says that even if the courts "were inclined to enlarge the remedy it could not be done in a case where the right is disputed, where no public interest is involved, where no reason is shown for a transfer of a specific and favorite thing, and where the remedy by action is fully adequate." *Townes v. Nichols*, 73 Me. 515 (1882), where the court vigorously says: "All the authorities declare that the remedy by mandamus cannot be resorted to in a case like this, unless the legal right of the petitioner to the possession of the thing sought for is clear and unquestionable. If there be doubt as to what his legal right may be, involving the necessity of litigation to settle it, mandamus must be withheld. Mandamus is the right arm of the law. Its principal office is not to inquire and investigate, but to command and execute. It is not designed to assume a part in ordinary law suits or equitable proceedings. It is properly called into requisition in cases where the law has been settled, or in

based largely on the historical origin of the writ of mandamus, and on the theory that the stock of a private corporation has no peculiar value and may be readily obtained in open market or fully compensated for in damages. It is doubted, however, whether these reasons will be sufficient to restrain the manifest tendency to enlarge the scope of this writ, particularly with reference to stock transactions. There is a strong list of decisions which hold that a mandamus lies to compel a corporation to allow a registry of a transfer of stock, particularly where the corporation has no good and sufficient reason for refusing the registry.¹ Perhaps the strongest argument against granting a mandamus for this purpose lies in the fact that by a bill in equity not only can a registry be specifically decreed and ordered by the court, but the rights of the corporation and any other claimant be fully and finally heard and disposed of. It has been held that mandamus will issue to aid the sheriff in transferring stock sold on an execution sale.² This rule, however, would work harshly in States where the purchaser of the outstanding certificate may have some rights, and where such a possibility exists the mandamus should be denied.³

cases where questions of law or equity cannot properly and reasonably arise. Its very nature implies that the law, although plain and clear, fails to be enforced and needs its assistance." See also *Rex v. Worcester Nav. Co.*, 1 Mon. & R. 529 (1828); *Queen v. Liverpool, M. & C. Ry. Co.*, 21 L. J. (Q. B.) 284 (1852); *Murray v. Stevens*, 110 Mass. 95 (1872), where the court says, in refusing a mandamus to compel a registry of stock: "Without undertaking to lay down an invariable rule on the subject, we think it must be said that this process was not intended and is not well adapted for the trial of mere questions of property." *State v. Warren Foundry & M. Co.*, 32 N. J. L. 439 (1868), where a previous transfer had been registered, although possibly in fraud of creditors. *Freon v. Carriage Co.*, 42 O. St. 30 (1884), refusing a mandamus, although it is said "that this stock has no market value, that the corporation is doing a growing and profitable business, that its good will enhances the value of the stock, and that by reason of these things damages will not be an adequate remedy. These facts do not change the rule. They are elements in assessing

damages, which may be fully ascertained in an action at law." See also *Pomeroy on Eq. Juris.* § 1412; *State v. People's Bldg. & C. Association*, 43 N. J. L. 389 (1881).

¹ *People v. Goss Mfg. Co.*, 99 Ill. 355 (1881); *State v. First Nat'l Bank*, 89 Ind. 302 (1883); *Green Mount & C. Co. v. Bulla*, 45 Ind. 1 (1873); *People v. Crockett*, 9 Cal. 112 (1858); *Townsend v. McIver*, 2 S. C. 25 (1870); *State v. Cheraw, & C. R. Co.*, 16 S. C. 524 (1881); *Cooper v. Swamp, & C. Co.*, 2 Murph. (S. C.) 195 (1812); *Norris v. Irish Land Co.*, 8 El. & Bl. 512 (1857); *Regina v. Carnatic Ry. Co.*, L. R. 8 Q. B. 299 (1873); *Crawford v. Prov. Ins. Co.*, 8 U. C. (C. P.) 263 (1859); *Goodwin v. Ottawa & P. Ry. Co.*, 13 U. C. (C. P.) 254 (1863), holding also that the mandamus may run to the corporation itself, without specifying any officers, and that an evasive answer by them is equivalent to a refusal to register.

² *State v. First National Bank, supra*; *Bailey v. Strohecker*, 38 Ga. 259 (1868).

³ *Durham v. Man. & C. Co.*, 9 Oreg. 41 (1880).

§ 391. *Remedy by suit in equity.*—This is, it seems, the surest, most complete, and most just remedy for compelling a corporation to register a transfer of stock, and for adjusting the various conflicting rights or claims of other parties.¹ It is a remedy applicable to almost all cases arising under a refusal of the corporation to allow a registry of transfer. The case will be decided on equitable principles, however, and a transfer will not be decreed if it involves bad faith.² The relief usually demanded is in the alternative, being either for a registry of the transfer or damages in lieu thereof. If all the stock has already been issued, equity has no power to compel a further issue.³

§ 392. *Remedy by an action for damages.*—An action at law for damages is an old and well established remedy of a stockholder who has applied to the corporation for a registry of a transfer and has been refused.⁴ The form of the action is not

¹ *Cushman v. Thayer Mfg. Co.*, 76 N. Y. 365 (1879), where the court says: "The right of the plaintiff to maintain this action depends upon the question whether an equitable action will lie to compel a transfer of stock by a corporation to the owner of the same, or the plaintiff must seek a remedy by an action at law for damages. The latter action is frequently of no avail and does not always afford complete and full redress. It is easy to see that a party may have become the owner or purchaser of stock in a corporation, which he desires to hold as a permanent investment, which may be at the time of little value, in fact without any market value whatever, and its real worth may consist in the prospective rise which the owner has reason to anticipate will follow from facts within his knowledge. To say that the holder shall not be entitled to the stock because the corporation without any just reason refuses to transfer it, and that he shall be left to pursue the remedy of an action for damages, in which he can recover only a nominal amount, would establish a rule which must work great injustice in many cases, and confer a power on corporate bodies which has no sanction in the law. A court of equity will enforce a specific performance on a contract for the sale of real estate, and compel the execution of a deed by the vendor to the vendee, although an action at law may be brought to recover

damages for the breach of the contract. Such a case bears a striking analogy to the one now presented, and the same principle is manifestly applicable where the remedy at law is inadequate to furnish the proper relief." *Walker v. Detroit Transit Ry. Co.* 47 Mich. 338; *Iasigi v. Chicago, B. & Q. R. R. Co.* 129 Mass. 46 (1880); *Mechanics Bk. v. Seton*, 1 Peters, 299 (1828); *Middlebrook v. Merchants Bk.*, 3 Abb. Ct. of App. 295 (1866); *Buckmaster v. Consumers Ice Co.*, 5 Daly, 513 (1874). *Iron R. R. Co. v. Fink*, 41 O. St. 321 (1884), the court saying that the power of equity to decree a registry is well settled. As regards the pleadings see *Burrall v. Bushwick R. R. Co.*, 75 N. Y. 211 (1878).

² *Regina v. Liverpool, &c. Ry.* 21 L. J. (Q. B.) 284.

³ *Smith v. North Am. Min. Co.*, 1 Nev. 423 (1865), and see § 284.

⁴ *Hussey v. Manufacturers & M. Bk.*, 27 Mass. 414 (1830); *Helm v. Swiggett*, 12 Ind. 194 (1859). Cases supporting this rule abound in all the States. They will be found together with others in the Chapter on the Measure of Damages. If the corporation illegally refuses to allow a registry, but afterwards does allow it, the corporation is not liable in damages for the decline of the market value of the stock in the meantime. *Skinner v. City of London M. Ins. Co.*, L. R. 14 Q. B. D. 882 (1885).

definitely fixed and in different States different forms seem to have been passed upon without any question being raised as to their technical nature.¹ The measure of damages is substantially the same as in other cases of conversion of stock.² The Statute of Limitations runs only from the time when a demand for registry was made.³

¹ See Chapter on Common Law Pleadings and Measure of Damages.

² *Id.*

³ *Cleveland R. R. Co. v. Robbins*, 35 O. St. 483; *Iron R. R. Co. v. Fink*, 41 O. St. 321 (1884).

CHAPTER XXIII.

RULES FOR CORPORATIONS IN REGARD TO REFUSING OR ALLOWING REGISTRIES OF TRANSFERS OF STOCK.

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| <p>§ 393. Purpose of the chapter.</p> <p>394. Right to refuse until the transferer pays the unpaid subscription price.</p> <p>395. Whether the corporation may refuse to register a transfer to an irresponsible transferee.</p> <p>396. Corporation may refuse to register as transferees persons who are incompetent to contract.</p> <p>397. Trustees, executors, guardians, agents, and pledgees.</p> <p>398. Sales of stock by executors or administrators.</p> <p>399. Sales by trustees.</p> <p>400. Sales by guardians.</p> <p>401. Forgery of transfer.</p> | <p>§ 402. Corporation must require a surrender of the outstanding certificate.</p> <p>403. Alleged loss of the old certificate.</p> <p>404. Attachment or execution.</p> <p>405. Decree of a court that certificates be issued.</p> <p>406. Theft of certificates indorsed in blank.</p> <p>407. Interpleader by the corporation.</p> <p>408. Restrictions by corporation on stockholder's right to sell or transfer.</p> <p>409. Lien of the corporation.</p> <p>410. Formalities of registry which the corporation may insist upon.</p> |
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§ 393. *Purpose of the chapter.*—It is proposed in this chapter, as a continuation of the last, and as a recapitulation of the various rights, liabilities, and duties of the corporation in refusing or allowing a registry of a transfer of stock, to state briefly the rules which prevail herein. The standpoint taken is that of the corporation. The minute and particular application of the general rules governing this subject are not stated here at length, but an effort has been made to give, in systematic order, certain directions which will enable a corporation, when in doubt as to whether to allow or refuse a registry, to decide the question intelligently and safely.

§ 394. *Right to refuse until the transferrer pays the unpaid subscription price.*¹—A corporation cannot refuse to register a transfer of stock, merely because the subscription price has not been fully paid in, unless the charter or the statutes of the State expressly give that right. Nor can it refuse registry, even though a call for part of the subscription price has been

¹ See Chapter XV.

made, is due, and remains unpaid. It must allow a registry but may continue to hold the transferrer liable for the call. The corporation has no lien on the stock for the subscription price, nor has it a right to restrict transfers until calls or parts of the subscription price not yet called are paid. The policy of the law is to favor the right of transfer, and no impediments by the corporation are allowed to restrict that right. As regards parts of the subscription not yet called in, the transferrer is released from liability and the transferee assumes the liability. As regards calls made before the application for registry, but not yet due, the transferrer is liable, but, it seems, not the transferee. As regards calls made before the application and due before such, the transferrer and not the transferee is liable. As regards calls made after the application the transferee alone is liable. In Pennsylvania, however, a different rule prevails, and the transferrer, if he is the original subscriber, is alone liable until the whole subscription is paid. In New York, by statute, both railroad and manufacturing corporations may refuse to allow registry of transfers, until unpaid calls have been paid.

§ 395. *Whether the corporation may refuse to register a transfer to an irresponsible transferee.*¹—Greater difficulty is experienced in finding a working rule on this subject. On one point, however, all the authorities agree. If the corporation is insolvent or in such a state of decline that insolvency seems inevitable, the corporation may refuse to allow a registry of transfer from a responsible to an irresponsible insolvent transferee. The policy of the law is to protect corporate creditors, even at the expense of restricting the right of transfer. The above rule applies not only where the subscription is unpaid, but also where it has been paid and only a statutory liability exists. Where, however, the corporation is solvent and a stockholder applies for a registry of transfer from himself to an irresponsible transferee, it seems that the corporation cannot refuse to make the registry.

§ 396. *Corporation may refuse to register as transferees persons who are incompetent to contract.*²—If the transferee of a certificate of stock is an infant, or person of unsound mind, the corporation may refuse to register such transferee as a stock-

¹ See Chapter XV.² See Chapter XIV.

holder. The reason of the rule is that such persons would not be obliged at law to respond to the obligations of a stockholder, and consequently are not entitled to its privileges. With married women at the present day, the law is different. At common law they were incompetent to become a stockholder, the same as an infant is at the present time. But the statutes of all the States have substantially removed these disabilities, and enabled a married woman to transact business as a *feme sole*, so far as her separate estate is concerned. She may become a stockholder in a corporation, but cannot bind her husband's estate for the liabilities of such stockholdership.

§ 397. *Trustees, executors, guardians, agents, pledgees.*¹—In registering transfer to a trustee, executor, or guardian, the corporation may be required to register the transferee as holder in his official capacity. A trustee who purchases or receives stock to hold in trust for the benefit of another, may, it seems, require the corporation to register the transfer and issue new certificates to himself, in his own name as "trustee." In England the rule appears to be different. The reason of this rule is that the liability of a trustee on stock, is in many of the States different from that of a complete owner of the stock, and also because where stock is held by a trustee, as trustee, it is the duty of the corporation to refuse to allow the trustee to sell and register a sale of the stock, unless the instrument creating the trust authorizes such sale. So also an executor, or administrator, or guardian, may compel the corporation to place his official title, after his name, in the stock registry. Pledgees, however, and agents, have not this right. The corporation need not write the word "pledgee" after the transferee's name, either in the stock registry or on the certificate. Such is the rule for the reason that the corporation is not obliged to protect the rights of the pledgor, nor to recognize the pledgeeship of the transferee. The same rule applies to transferees who take as agents of the transferrer.

§ 398. *Sales of stock by executors or administrators.*²—A corporation may with safety, and in fact is obliged to allow an executor or administrator to register a transfer of the sale of stock

¹ See Chapter XIV.

² See Chapter XIX.

belonging to the estate, upon presentation by the executor or administrator of the letters testamentary or letters of administration. The executor or administrator may then register a transfer of the stock to himself, or directly from the name of the deceased to a purchaser from the executor; or from the deceased to the executor, and then from the executor to the purchaser. One executor may sell and register a transfer of the stock. The corporation is not bound to inquire whether it is necessary that the sale be made in order to pay the debts of the estate, nor to see to it that the executor actually applies the proceeds of the sale to that purpose. Where, however, the corporation has actual knowledge, through its officers that a breach of trust is contemplated by the executor, it is bound to refuse registry and will be liable to the estate for neglecting so to do. So also where such a long time has elapsed between the taking out of the letters and the sale by the executor, that the latter has become practically a trustee, the corporation must use the same precaution as in sales by a trustee. In the case of specific legacies of stock, the corporation need take no notice of them, but must allow the executor to transfer the stock into his own name, since he may need it to pay debts, and the corporation is not bound to investigate such questions.

§ 399. *Sales by trustees.*¹—A trustee who holds stock belonging to the trust estate has no right to sell and transfer such stock unless he is expressly authorized so to do by the instrument creating the trust. Consequently the law imposes upon the corporation the duty of refusing to allow a trustee to transfer the stock unless he clearly has a right so to do. If the corporation neglects this duty it is liable to the trust estate, and in case of a breach of trust by the trustee, may be compelled to replace the stock or pay damages. If the trustee has an express power given to him to sell, the corporation may allow him to make the transfer. If no such power is given, the corporation must refuse. The trustee is bound to reasonably satisfy the corporation of his right, but the corporation cannot permanently retain the papers submitted to it for that purpose.

§ 400. *Sales by guardians.*¹—A guardian has a right to hang the investment of the funds in his charge, and consequent-

¹ See Chapter XIX.

ly has a right to sell stock held by him in his official capacity. Accordingly, the corporation may allow him to register a transfer of stock held by him as guardian, and cannot require the guardian to obtain an order or decree from a court authorizing such transfer. An order or decree is often obtained by the guardian, however, for his own protection, and is to be commended. In New York, the rights and duties of guardians are regulated by statute, and other States have similar statutes.

§ 401. *Forgery of transfer.*—A corporation is bound and required to detect a forgery, whereby the name of the owner of a certificate of stock is signed to it, and a transfer made which the corporation is requested to register. The stockholder in whose name the old certificate was made out, and whose name was forged to the transfer, may hold the corporation liable if it fails to detect the forgery and allows a registry of the forged transfer. He may compel it to replace the stock or pay damages. This rule is due to the fact that the corporation is a custodian of the books whereby a stockholder obtains his rights of stockholdership, and it cannot deprive him of these rights by allowing others to take them from him by the aid of the corporation and without his consent. It is in the power of the corporation to require the presence of the transferrer at the time of registry, or at least clear proof that the signature is genuine. The corporation, however, has recourse over against the person who applied for registry on the forged transfer, however innocent the latter may be. He is held to have impliedly represented that the transfer was genuine.

§ 402. *Corporation must require a surrender of the outstanding certificate.*¹—If a corporation permits a registry of a transfer of stock, and issues new certificates to the transferrer without requiring a surrender of the old certificate, it assumes a dangerous position, and one which it is not obliged to assume. If the certificate which is not delivered up is in the hands of a *bona fide* purchaser for value, and without notice, he may hold the corporation liable for allowing a registry of transfer to another without requiring a delivery of the certificates. It is negligence and a breach of duty on the part of the corporation to allow a

¹ See Chapter XXI.

registry without a surrender of the old certificate. It generally refuses to do so, as is its duty, and is sustained by the law in its refusal. There are occasions, however, where the law compels the corporation to register the transfer without a surrender of the old certificate. When so compelled to do, the corporation cannot be held liable by the purchaser of the outstanding certificate, but he must seek his remedy against others. Such compulsory registry, excusing the corporation, may exist in cases of alleged loss of the old certificate; a decree of a court compelling the registry; and, under the latter, an attachment or execution against the stock.

§ 403. *Alleged loss of the old certificate.*¹—A corporation is not, according to the rule of nearly all the States, obliged to issue a new certificate of stock to the owner of an old one, which he alleges that he has lost, unless such person gives to the corporation a sufficient bond of indemnity to protect it against liability in case it turns out that the old certificate was not lost, but was sold and passed into *bona fide* hands. In New York this rule is fixed by statute. The corporation is liable to the holder of the outstanding certificate, if it is outstanding, and, consequently, should be protected against that liability by a bond from the applicant for registry. In Louisiana a statutory advertisement is made, and a bond of indemnity dispensed with. But in the other States the court compels the loser to give a bond, varying in amount according to the amount of the stock and the clearness of the proof of loss.

§ 404. *Attachment or execution.*²—Nearly all the States have laws whereby shares of stock are rendered subject to levy of attachment, and to sale on levy of execution. Such attachment or execution can be levied only at the domicile of the corporation, since the certificates are mere evidence of title, and the *res* itself of the stock exists only where the corporation is created. When, therefore, an execution sale, or an attachment followed by an execution sale, takes place where the corporation exists, the purchaser at such sale generally has not the outstanding certificate, but, nevertheless demands registry of himself as stockholder in accordance with the law authorizing the attachment and execution.

¹ See Chapter XXI.

² See Chapter XXVII.

In the meantime the judgment debtor, whose stock is thus attached or sold under an execution, generally has sold or will sell his certificate of stock to a *bona fide* purchaser for value. If it happens that both parties claim the stock, the duty and privilege of the corporation is plain. It may refuse to decide between them, and when sued by either may interplead and compel the claimants to settle the right between them in the courts. But frequently it happens that the corporation does not know whether the judgment debtor has sold the outstanding certificate or not. By the law of most of the States, if such certificate was sold before the attachment or execution was levied, the purchaser would be protected, and the corporation would be liable to him for registering as a stockholder the purchaser at the execution sale. Accordingly, in that case it is the duty of the corporation to refuse to register the purchaser at the execution sale. It cannot afford to take the risk, and is not obliged to take it. If the court then compels it to make the registry of transfer to the execution purchaser, the court will also, probably, compel such purchaser to give a bond of indemnity to protect the corporation. If such a bond is not required by the court, the corporation must nevertheless obey the decree. What rights the purchaser of the outstanding certificate would then have has not as yet been passed upon by the courts.

§ 405. *Decree of a court that certificates be issued.*¹—A corporation must, of course, obey the decree of a court that it issue a certificate of stock to a specified person. But a court will rarely resort to such an extreme remedy where it is probable or possible that there may be an outstanding certificate in the hands of an innocent holder representing the same shares. As a principle of law, the court has no power to decree such an issue ordinarily, since the whole capital stock has been issued, and its decree amounts practically to an order to make an overissue of stock. Generally the court decrees damages to be paid, or directs the corporation to purchase stock for the purpose of reissuing it to the specified party. This occurs frequently where the corporation has unjustly deprived a person of his stock. A different class of cases arise where the corporation has refused to allow a registry because the outstanding certificate is not surrendered. Such cases include those of alleged loss of certificate, an execu-

¹ See Chapter XXII.

tion sale of the stock, and, possibly, a suit in equity at the domicile of the corporation to recover from another stock which the complainant claims. A decree in such a suit in most States would be ineffectual to deprive of his rights one who purchased from the defendant his certificate of stock before the decree was rendered. It would, accordingly, be a harsh decree that compelled the corporation to register the successful complainant as a stockholder. The corporation should not be compelled to assume the risk of being sued by the purchaser of the outstanding certificate. The complainant should be compelled to give a bond of indemnity, or else be contented with a personal judgment against the defendant. The demands of trade and of an investing public require that the safety of a purchaser of a certificate of stock should be assured, except against attachments, execution sales, or decrees duly obtained and notified to the corporation before the *bona fide* purchaser received the certificate of stock.

§ 406. *Theft of certificates indorsed in blank.*¹—The corporation has a duty to perform as regards certificates of stock which have been stolen from the owner, who held them indorsed in blank.

If the owner notified the corporation of the theft it must refuse to register a transfer to a purchaser of such stolen certificate. Since the owner's negligence may have estopped him from reclaiming the stock, the corporation may refuse to recognize either party as a stockholder, where there is a reasonable question of negligence, and when sued by either may interplead. If the corporation allowed a registry before it was notified of the theft, it is difficult to see on what principle it is to be held liable to the owner. Such a case seems not yet to have arisen. If notified of the theft before anything is learned concerning the whereabouts of the certificate, the case is to be treated the same as when the certificate is alleged to have been lost.

§ 407. *Interpleader by the corporation.*²—Whenever there are two or more conflicting claims made to stock and demands are made on the corporation to allow registry, it is the privilege of the corporation, if there is a reasonable legal doubt as to the rights of the parties, to refuse to register either party, and

¹ See Chapter XXI.

² See Chapter XXII.

when sued by one to interplead and compel the parties to contest the matter between themselves in the courts. The law does not oblige the corporation to turn itself into a court of justice and decide the rights of the parties. The corporation, however, cannot interplead, if it has already committed itself by registering one of the claimants as the stockholder. Nor can the corporation resort to an interpleader where one of the claimants is clearly wrong. The right of interpleader and the power of the corporation to refuse to register a transfer, until compelled to do so by the courts, where an outstanding certificate is not surrendered, constitutes the two most effective safeguards of the corporation in allowing or refusing registry.

§ 408. *Restrictions by corporation on stockholder's right to sell or transfer.*¹—The law has uniformly and decisively discountenanced and overruled all attempts of a corporation to prevent the sale and transfer of its stock by the stockholder. Such attempted restrictions are generally made by means of by-laws. Thus a by-law requiring the consent of the directors or other corporate officers to a transfer, or a by-law requiring the stockholder, when he sells, to sell his stock to specified persons, is null and void. Restrictions may be created by a contract mutually agreed to by the stockholders, but cannot be imposed upon them by the majority of the stockholders nor by the board of directors. When, however, such restrictions are created by the charter, they are valid, since they arise with the corporation and stock itself. Thus, in England, the charter frequently authorizes the directors to refuse a registry unless the transferee is satisfactory to them. Even here, however, the directors must be reasonable in the use of their discretion. In this country the most frequent restrictions created by charter is that of a lien for debts due to the corporation from the transferer.

§ 409. *Lien of the corporation.*²—The charters of many corporations contain an express provision that the corporation may refuse to allow a stockholder to register a transfer of his stock, until he has paid any and all debts which he may, at that time, owe to the corporation. Such a lien need not be stated in the certificate of stock. While it may not be created generally by a

¹ See Chapter XX.

² See Chapter XXXI.

by-law, yet certain phrases in charters have been held to uphold a lien that is declared and made effectual by a by-law. Where the line exists the corporation may refuse to allow a registry of transfer of any stock owned by the debtor until all debts due from him to the corporation are paid, whether due or not due, including, it seems, unpaid subscriptions. It does not apply, however, to debts due from a transferee of the certificate who never obtained registry or appeared as a stockholder on the corporate books. Nor does it apply to debts due from the registered stockholder, but incurred after the corporation was given notice that he had sold his stock to another. The corporation may waive its lien, and allow registry without the debts of the old stockholder being paid. A registry, without requiring payment, is a waiver in itself.

§ 410. *Formalities of registry which the corporation may insist upon.*¹—Where, as is ordinarily the case, the owner of stock has sold it by signing the transfer and power of attorney on the back of the certificate, leaving the names of the transferee and of the attorney blank, the corporation may require the names of the transferee and of the attorney to be filled in before it allows a registry. If it is in doubt as to the genuineness of the signature of the former owner of the certificate, it may require his presence or reasonable proof that he actually made the signature. It cannot compel the transferrer to be present, but may require the presence of the attorney authorized to make the registry. The registry itself is generally made by the corporate officer, but he may require the attorney to make it. A surrender of the old certificate is required, and new certificates in the name of the transferee are issued. The by-laws may prescribe that the registry shall be in the presence of certain corporate officers. A mere request to register is not registry, although the old certificate is left with the clerk, together with the transfer, and he marks “received for record” on the same. The applicant may inquire of the corporate officer in charge for the registry clerk, and is not bound to ascertain the individual himself. Registry at a branch office is not a legal registry, until entered at the main office. The corporate registry may be on its ledger, without any issue of certificate. If it keeps no registry at all, mere notice to it of a transfer constitutes a legal registry. The corporation has no

¹ See Chapter XXII.

right to delay registry unreasonably for the purpose of obtaining advice or for any other reasons. It may require that the power of attorney run directly from the former registered stockholder, and not from an intermediate one. A written acceptance of the stock by the transferee cannot be insisted on by the corporation. The formalities of registry may be waived by the corporation, and any act which indicates that it considers a transferee to be a stockholder is effectual to make him such so far as the corporation is concerned, though no registry was had.

Either the transferrer or the transferee, or an intermediate unregistered transferee, may apply to the corporation for the purpose of obtaining a registry. The corporation cannot refuse it, merely because of the motion of the transferrer or of the transferee in making the sale and transfer. Whenever the corporation refuses to allow a registry, the applicant may sue it for damages, or he may go into a court of equity and ask that the corporation be decreed to allow registry or to pay damages in lieu thereof. A few cases hold that he may compel registry by a *mandamus* against the corporation, but the weight of authority holds otherwise.

CHAPTER XXIV.

NON-NEGOTIABILITY OF STOCK AND DANGERS INCURRED IN THE PURCHASE OF CERTIFICATES OF STOCK.

A.—NON-NEGOTIABILITY.

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B.—DANGERS INCURRED IN PURCHASING STOCK.

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A.—NON-NEGOTIABILITY.

§ 411. *Nature and kinds of negotiable instruments.*—Negotiable instruments at the present day are promissory notes; bills of exchange; checks; bank-notes; bonds of the United States, States, foreign governments, municipalities, cities and counties;

railroad bonds; certificates of deposit; and interest coupons.¹ Bills of lading have only a quasi-negotiability.² These different instruments, however, are not necessarily negotiable, but are so only when in writing; when containing an unconditional promise or order to pay; when the payment is to be in money only; when the amount is certain; when it is payable to a specific person, and not in the alternative; when it is payable at a certain time; when it contains words such as "to A. or order," or "to bearer," or their equivalent; and when delivery has been duly made.³ If the instrument is lacking in any one of these qualities it falls back into the category of non-negotiable, that is merely assignable, instruments. Again, a holder of one of the above-named negotiable instruments, can have the benefit of its negotiability only when he has purchased it in good faith, for value, and without notice of the equitable rights of previous holders or makers; that is, he must be a *bona fide* holder. When all these elements of negotiability and ownership co-exist, the advantage of negotiability over non-negotiability is this, that the holder of the instrument is entitled to the face value thereof, and his right cannot be affected, decreased, or defeated by any facts or equities between previous holders, which would defeat the security as between them, unless it be void for usury or other similar cause.

§ 412. *Certificates of stock are not negotiable instruments.*—

It is very clear, and it is well established, that certificates of stock are not negotiable instruments.⁴ A certificate of stock is not a

¹ 1 Daniel on Negotiable Instruments, 3d ed.; Das Passos on Stock Brokers, Ch. IX.

² Id.

³ Id.

⁴ "Certificates of stock are not securities for money in any sense, much less are they negotiable securities." *Mechanics Bk. v. New York & N. H. R. R. Co.*, 13 N. Y. 599, 627 (1856); *Barstow v. Savage M. Co.*, 64 Cal. 391 (1883); *Weaver v. Barden*, 49 N. Y. 286, 288 (1872), says that a certificate of stock has none of the qualities of commercial or negotiable paper. *Leitch v. Wells*, 48 N. Y. 585, 613 (1872), says: "Since the decision of the case of *McNeil v. Tenth National Bank*, . . . certificates of stock, with blank assignments, and powers of attorney attached, must be nearly as negotiable as commercial paper." *Weyer v. Second*

Natl. Bk., 57 Ind. 198, 208 (1877), says: "The difference between a promissory note and a certificate of bank stock, is so wide and marked, that a rule of law governing the transfer of the former, is by no means applicable to the latter." *Sewall v. Boston Water Power Co.*, 86 Mass. 277 (1862), says: "The authorities cited, show that a certificate of stock is not a negotiable instrument, and without any authorities, it is apparent that it has not a negotiable character." To same effect *Mandlebaum v. North Am. Min. Co.*, 4 Mich. 465, 473 (1857), holding, however, that by statute in that State, certificates of stock are practically negotiable. *Shaw v. Spencer*, 100 Mass. 382 (1868), says: "It is clear that a certificate of stock, transferred in blank, is not a negotiable instrument. . . . No commercial usage can give to such an instrument the attri-

promise or order to pay money, nor has it any of the essentials of a negotiable instrument, except that delivery must be made in order to render it valid. Moreover, it has been repeatedly decided by the courts, that a certificate of stock is not negotiable, and no custom of trade or of brokers can give to it that character.

§ 413. *The term "quasi-negotiability" as applied to certificates of stock, throws little light upon the subject.*¹—It is little satisfaction to the court, the practitioner, the student, or the owner of stocks to be told that certificates of stock have a quasi-negotiability. The term itself has been coined to describe the character of certain things which can be understood only by a study and knowledge of the characteristics of the thing described. Especially is this true of certificates of stock. The information sought for is not whether the certificate is quasi-negotiable, but whether the holder of it is protected under different states of fact and circumstances. He who intends to purchase such certificates, wishes to know what dangers or risks he incurs by the purchase. The practitioner is interested, not in the general character of the instrument, but in the law as applicable to his particular case. Many of the cases concede to certificates of stock a quasi-negotiability, but it is extremely doubtful whether such discussions do not confuse the understanding of the character of such an instrument, more than they explain it.

§ 414. *The distinction between the "legal" and the "equitable" title in the transfer of certificates of stock is unsatisfactory.*—Many of the cases involving the rights of a transferee of stock, discuss and treat the subject from the point of view that

butes of negotiability." *Sherwood v. Meadow Valley M. Co.*, 50 Cal. 412 (1875); *Bridgeport Bk. v. New York & N. H. R. R. Co.*, 30 Conn. 231, 275 (1871), says: "The certificate accompanied by the assignment and power of attorney thus executed in blank, has, perhaps, a species of negotiability, although of a peculiar character, but one necessary to the public convenience." In *Bank v. Lanier*, 11 Wall. 369, 377, the court says, that although certificates of stock "neither in form or character are negotiable paper, they approximate to it as nearly as practicable."

¹ Daniel on Negotiable Instruments, § 1708, says: "The phrase 'quasi-negotiability,' has been termed an unhappy one, and certainly it is far from satisfactory, as it conveys no accurate, well defined meaning. But still it describes better than any other shorthand expression, the nature of those instruments which, while not negotiable in the sense of the law merchant, are so framed and so dealt with as frequently to convey as good a title to the transferee as if they were negotiable."

the transferee is protected in his ownership when the legal title passes to him, but is not so protected when only the equitable title passes. Unfortunately, it happens that under the same state of facts, one court will hold that only the equitable title passes; another that the legal title passes; and a third court will hold that both the legal and equitable passes. The result is confusion, doubt and difficulty with little light as to the real *status* of certificates of stock.¹

§ 415. *The only method of treatment of the subject seems to be by inquiring under what facts the holder or purchaser is protected.*—The court, the practitioner, the purchaser, and the

¹ Such also seems to be the view taken in *Lowell on Transfer of Stock* (1884), p. 105, where the learned authors say: "It is often supposed, for example, that the right of a creditor to seize stock which has been sold before it is transferred upon the books, depends upon the passing of the legal title, but we shall attempt to prove that the legal title has in reality no effect upon the matter." The same authority shows the confusion resulting from this distinction of the legal from the equitable title, in the following note to page 103: "That the legal title passes before the transfer on the books. In the following cases this is made part of the *ratio decidendi*: *Ross v. Southwestern R. Co.*, 53 Ga. 514, 532; *Merchants' Nat. Bank v. Richards*, 6 Mo. App. 454, 463; *s. c.* 74 Mo. 77; *Carroll v. Mullanphy Savings Bank*, 8 Mo. App. 249, 252. *McNeil v. Tenth Nat. Bank*, 46 N. Y. 325; *Leitch v. Wells*, 48 N. Y. 585; *Smith v. American Coal Co.*, 7 Lans. 317; *Noyes v. Spaulding*, 27 Vt. 420; *Cherry v. Frost*, 7 Lea, 1. In the following cases the same principle was laid down *obiter*: *State v. Leete*, 16 Nev. 242, 250; *Eastman v. Fiske*, 9 N. H. 182; *New York, &c. R. v. Schuyler*, 34 N. Y. 30, 80; *Grymes v. Home*, 49 N. Y. 17; *Johnson v. Underhill*, 52 N. Y. 203; *Holbrook v. New Jersey Zinc Co.*, 57 N. Y. 616; *Cushman v. Thayer Mfg. Co.*, 76 N. Y. 365, and see *Purchase v. Exchange Bk.*, 3 Rob. 164.

That the legal title does not pass until transfer on the books. In the following cases this principle is made of the *ratio decidendi*: *Union Bank v. Laird*, 2 Wheat. 390; *Lowry v. Commercial Bank*, Taney, 310; *Brown v. Adams*, 5 Biss. 181; *Williams v. Mechanics' Bank*, 5 Blatch.

59; *Becher v. Wells Flour & Mill Co.*, 1 Fed. Rep. 276; *Marlborough Mfg. Co. v. Smith*, 2 Conn. 579; *Northrop v. Newtown & Bridgeport Turnpike Co.*, 3 Conn. 544; *Oxford Turnpike Co. v. Bunnell*, 6 Conn. 552; *Dutton v. Connecticut Bk.* 13 Conn. 493; *Vansands v. Middlesex Co. Bk.*, 26 Conn. 144; *Coleman v. Spencer*, 5 Blackf. 197; *Helm v. Swiggett*, 12 Ind. 194 (*semble*); *Weyer v. Second Nat. Bk. of Franklin*, 57 Ind. 198; *Fisher v. Essex Bk.*, 5 Gray, 373; *Boyd v. Rockport Steam Cotton Mills*, 7 Gray, 406; *Blanchard v. Dedham Gas Co.*, 12 Gray, 213; *McCourry v. Suydam*, 5 Halst. 245; . . . *Stebbins v. Phoenix Ins. Co.*, 3 Paige, 350; *Mechanics' Bk. v. New York, &c. R. Co.*, 13 N. Y. 599; *New York, &c. R. Co. v. Schuyler*, 38 Barb. 534; *Lockwood v. Mechanics' Nat. Bk.*, 9 R. I., 308, 331, 335.

"In the following cases the same doctrine is laid down *obiter*: *Black v. Zacharie*, 6 How. 483; *United States v. Cutts*, 1 Sumner, 133 (this was, however, a case of government debt, not of corporate stock); *Planters' & Merchants' Ins. Co. v. Selma Savings Bk.*, 63 Ala. 585; *Otis v. Gardner*, 105 Ill. 436 (*semble*), and see *Kellogg v. Stockwell*, 75 Ill. 68; *People's Bk. v. Gridley*, 91 Ill. 457; *Bruce v. Smith*, 44 Ind. 1; *State v. First Nat. Bk. of Jeffersonville*, 89 Ind. 302; *Shaw v. Spencer*, 100 Mass. 382; *Sibley v. Quinsigamond Nat. Bk.* 133 Mass. 515; *White v. Salisbury*, 33 Mo. 150; *Boatmen's Ins. Co. v. Able*, 48 Mo. 136; . . . *Conant v. Seneca Co. Bk.*, 1 O. St. 298; *United States v. Vaughan*, 3 Binn. 394 (*semble*); *Bk. of Commerce's Appeal*, 73 Pa. St. 59; *Fraser v. Charleston*, 11 S. C. 486 (*semble*)."

holder of certificates of stock wishes to know what liability, and what dangers, are incurred by the purchase and ownership of a certificate of stock. It becomes important for him to ascertain whether forgery; or theft; or improper registry by the corporation; or breach of trust by a trustee, executor, or agent, formerly holding that particular stock; or fraud whereby a former owner was deprived of that same stock; or legal proceedings, such as attachment, execution, mandamus, and decrees of the court; or any other fact or equitable right between former owners of the stock which he purchases can affect him, a *bona fide* purchaser for value and without notice of those rights. These questions cannot be solved or answered by any general rules or theories, since certificates of stock have a law, an origin, and a nature different from other kinds of securities. The fact that a registry of transfer is required to be made on the corporate books adds further complication to the rights of a holder. General rules formed from and applicable to other instruments or securities cannot with any certainty, clearness, or satisfactory results, be applied to certificates of stock. They should be treated of by themselves. It is also to be observed that the future character and *status* of certificates of stock will be much clearer, better, and more satisfactory to the investing public, if the law governing them be formed on its own basis.

§ 416. *The particular rules protecting a bona fide purchaser of certificates of stock are based on estoppel.*—Nearly all, if not all of the rules whereby a purchaser of stock is protected against the equitable rights of previous holders, grow out of the fact that such previous holder or holders have enabled persons to sell the stock and consequently are estopped from claiming that they did not intend so to do.¹ This law of estop-

¹ In Wood's Appeal, 92 Penn. St. 379, 390 (1880), the court says: "The rights of a *bona fide* holder as against the true owner of the stock, to whom the apparent owner has either sold or pledged, do not depend on a negotiable character in the certificates, but rest on another principle, namely, that one who has conferred upon another by a written transfer all the *indicia* of ownership of property, is estopped to assert title to it as against a third person, who has in good faith purchased it for value from the apparent

owner. As a general rule, the vendor or pledgee can convey no greater right or title than he has. Simply intrusting the possession of a chattel to another as a depositary, pledgee, or other bailee, is insufficient to prevent the real owner reclaiming his property in case of an unauthorized disposition of it by the person so intrusted. The mere possession of chattels, without evidence of property or authority to sell from the owner, will not enable the possessor to give good title. But if the owner intrusts to another

pel protects the purchaser against not only the rights of previous holders, but against the claims of the corporation itself. Indeed, to such an extent has the law of estoppel been applied to protect a *bona fide* purchaser of stock, that he is protected now in almost every instance where he would be protected if he were purchasing a promissory note or other negotiable instrument. The courts are steadily extending the application of the law of estoppel herein, and in the course of time, it is possible that certificates of stock may become more negotiable than negotiable instruments themselves.

er the possession of property, and also written evidence of title and power of disposition over it, as respects innocent third persons, he is deemed as intending it shall be disposed of at the pleasure of the depository." *McNeil v. Tenth Nat. Bank*, 46 N. Y. 325, 329 (1871), says that "where the true owner holds out another, or allows him to appear as the owner of, or as having full power of disposition over the property, and innocent third parties are thus led into dealings with such apparent owner, they will be protected. Their rights in such cases do not depend upon the actual title or authority of the party with whom they deal directly, but are derived from the act of the real owner, which precludes him from disputing as against them, the existence of the title or power which, through negligence or mistaken confidence, he caused or allowed to be vested in the party making the conveyance." In *Weaver v. Barden*, 49 N. Y. 286, 287 (1872), the court said: "As a rule the purchaser or assignee of shares of the capital stock in a corporation acquires no other or better title than the seller or assignor has, and takes it subject to the legal and equitable rights of third persons. The rightful owner may be estopped by his own acts from asserting his title, as he may be in respect to other property of a like character. If he has invested another with the usual evidence of title, or an apparent authority to dispose of it, he will not be allowed to make claim against an innocent purchaser dealing upon the faith of such apparent ownership, and *jus disponendi*." To same effect *Moore v. Metropolitan Nat. Bk.*, 55 N. Y. 41, 47 (1873); *Mount Holly, &c. Co. v. Ferrie*, 17 N. J. Eq. 117 (1864). The result of the law of estoppel herein is well stated in *Walker v. De-*

troit Transit Ry. Co., 47 Mich. 338, 347 (1882). "These propositions are admitted: first that possession of certificates of corporate stock which bear the proper indorsements is *prima facie* evidence of ownership, and that the holder for value without notice of prior equities obtains a perfect title as against such equities; second, that if the rightful owner has invested another with the usual evidence of title, or an apparent authority to dispose of the stock, he will be estopped from making any claim against an innocent purchaser dealing on the faith of such apparent ownership or right of disposal." See also *Fatman v. Lobach*, 1 Duer, 354 (1852); *Moodie v. Seventh Nat. Bk.*, 3 W. N. C. 118 (1881); *Matthews v. Mass. Nat. Bk.*, 1 Holmes, 396 (1874). In England, certificates of stock indorsed in blank convey title by estoppel to a *bona fide* purchaser when the transfer need not be by deed under seal. *Rumball v. Metropolitan Bk.*, L. R., 2 Q. B. D. 194 (1877). *Ex parte Sargent*, L. R. 17 Eq. 273 (1873). But this is generally not the case. *Ortigosa v. Brown*, 47 L. J. (Ch.) 168 (1877); *Donaldson v. Gillott*, L. R. 3 Eq. 274 (1866), and the late case of *France v. Clark*, L. R. 22 Ch. D. 830 (1883), gives no protection to the *bona fide* purchaser until he is registered. See also *Shropshire, &c. Co. v. Queen*, L. R., 7 H. L. 496 (1875). In *Briggs v. Massey*, 42 L. T. 49 (1880), the following rule from Lindley's work on Partnership is approved: "Where the legal ownership in shares, or even only the legal right to be registered, is acquired by a *bona fide* purchaser for value without notice of a prior equitable interest, the title of such purchaser cannot be impeached in equity any more than at law."

B.—DANGERS INCURRED IN PURCHASING STOCK.

§ 417. *Liabilities, risks, and rights of one who owns or purchases a certificate of stock.*—It is proposed to state separately and in detail the liabilities on the subscription price and by statute incurred by one who owns or purchases a certificate of stock; also the risks or dangers incurred by a purchase of stock, as affected by the rights of previous holders of that stock; also a few of the rights of an owner or purchaser of a certificate of stock as regards the general incidents appertaining to stockholdership. These subjects are discussed in full in other parts of this work, and consequently the authority for rules laid down herein must be sought for in those parts. The purpose here is to state succinctly and in language free from technical phraseology the position occupied by a *bona fide* purchaser of a certificate of stock.

§ 418. *Liability on unpaid par value, that is the unpaid subscription price of the stock.*¹—In general the purchaser of a certificate of stock is immediately liable on the subscription price of the stock, so far as it has not been paid by previous holders of the stock purchased, and has not been called by the corporation. The transferrer is bound to pay all calls made before the transferee purchases. If the transferee does not immediately register his transfer on the corporate books he is liable to pay to the transferrer such calls as are made after the transfer and which the corporation compels the latter to pay. The transferee, it seems, is liable for uncalled and unpaid parts of the subscription, even though the certificate is silent as to whether the par value of the stock has been paid in or not. Where, however, the certificate states that the stock is paid up stock, or the transferee before purchasing inquires of the corporation and is told that the stock is paid up, he may purchase in reliance thereon, and cannot afterwards be held liable, even though the stock turns out not to have been fully paid up.

§ 419. *Forfeiture for non payment of calls.*²—Where the corporation is given by its charter, or by statute, the right to forfeit and sell stock for non-payment of the subscription price, when called in by the corporation, a notice to the stockholder of the intended forfeiture is always required. This notice, however, is

¹ See Chapter XV.² See Chapter VIII.

given always to him who appears, by the corporate registry, to be the stockholders. Accordingly a transferee or owner of stock, who has not obtained a registry of his transfer on the corporate books, is liable to lose his stock by a forfeiture for non-payment of calls, and may lose it without knowledge of the call or forfeiture unless he appears on the registry of the corporation as the owner of the stock.

§ 420. *Statutory liability*.¹—The liability, by statute, of a purchaser of certificates of stock to corporate creditors, in addition to the subscription price which is treated of above, exists in a great many cases. In the first place this liability may not exist at all against any one, either transferrer or transferee. It rarely, if ever, exists in the case of railroad corporations. In manufacturing corporations in New York the statute of 1848, which has been copied by most of the States of the Union, provides that *until* the whole capital stock has been paid in and a certificate to that effect filed, the stockholders are liable not only for the subscription price, so far as unpaid, but also to corporate creditors for an amount additional and equal to the par value of the stock. But the creditor's debt must have been payable within one year from the time it was contracted, and must be sued on within one year from the time when it was due. In national banks the stockholders are liable individually to corporate creditors, for not only the unpaid subscription price, but also for an amount in addition to and equal to the par value of the stock. In New York banking associations, other than national banks, there is no statutory liability, unless expressly stated in the articles of association of the bank. Where the statutory liability exists the liability of a purchaser of stock is as follows: If the transferee immediately registers his transfer on the corporate books he becomes at once liable by statute for debts of the corporation contracted after such registry, and the transferrer is not liable thereon. The transferee may or may not be liable on corporate debts contracted before he purchased, according to the words of the statute creating the liability. He, however, is liable for debts contracted after he purchased but before he registered the transfer. The transferrer is also liable in the latter case, but has recourse to his transferee.

¹ See Chapter XII.

§ 421. *Liability where the purchaser has the transfer made to a nominal holder.*¹—The law is not clearly settled as to whether the real purchaser is liable on stock which he as the transferer transfers to the name of another who acts merely as a man of straw for the real purchaser. Such arrangements are not necessarily fraudulent and they are of constant occurrence in business communities. The courts, however, do not favor them, and in several instances have disregarded the dummy and held the real owners liable on the ground that a principal is liable on the contracts of his agent. But in these cases generally an element of fraud on the public was involved. It may be said that the question whether any and all such arrangements will be disregarded by the courts is still an open one, with a strong probability in America, that for the benefit of corporate creditors the nominal holder will be passed over and the real owner held liable. Such certainly is the rule where a person transfers from himself to one who takes title nominally only and holds it for the benefit of the transferer. The dummy is, of course, liable on the stock, and if legal proceedings succeed in obtaining anything from him he has recourse to the real owner.

§ 422. *No liability for assessments after the par value of stock has been paid in.*²—By well established principles of law stockholders are liable on their stock only to the extent of the unpaid par value of the stock, unless the statute expressly provides otherwise. Neither the directors, nor all the other stockholders combined, in corporate meeting assembled or otherwise, can compel a dissenting stockholder to pay any more money into the corporation or subject him to further liability on his stock. Nor can the legislature subsequently to his purchase of the stock pass a law increasing his liability, unless the power to alter or amend the charter is reserved to it, in which case such a law would be constitutional.

§ 423. *Liability when stock was issued for property.*³—Shares of stock may be issued under an agreement that payment is to be made in labor services, material, or contract work. If so issued, and the labor or material received by the corporation is fairly equal in value to the par value of the stock, the transferee of such stock takes it as full paid stock, and cannot be held liable

¹ See §§ 249, 253.

² See Chapter XIII.

³ See Chapters II and III.

for any further amount, even though the estimate of the value of the property turns out subsequently to have been overestimated, but was made in good faith. Where, however, the property is intentionally overvalued, and stock is issued for it, the persons receiving the stock are liable to have the transaction set aside, the value of the property or work done credited to them, and the real value of the stock, not necessarily the par value, charged to them, or be compelled to return the stock. As to transferees, the case may be different. If they purchased with notice of the fraud, they are not protected; but if they purchased without notice or knowledge that the property was intentionally overvalued, but supposed that the stock was issued as paid up, by payment in property or work, taken at a *bona fide* value, or if they have no knowledge of how the stock was paid, but take it as paid up stock, they may retain the stock, and are not liable for any further amount thereon.

§ 424. *Liability as partners by reason of defective incorporation, or for other reasons.*¹—Where a supposed corporation has not been duly incorporated, owing to a failure of the incorporators to comply with the statutory requisites, or because a corporation for that business is not provided for, the supposed corporation is but a partnership, and all the stockholders are liable as partners. Any creditor of the assumed corporation may sue the stockholders as partners, and is not estopped from so doing. A failure to file the articles of association, or to sign and publish them, or the omission from them of any of the essential facts required to be stated, may defeat the attempted incorporation and render the stockholders liable as partners. Again, the stockholders are, in some jurisdictions, liable to be held to be partners, as regards creditors of the enterprise, where the corporation organizes in one place and proceeds to do all its business in another place. This is a migration of the corporation, and its corporate character is respected and recognized only by the comity of the States, and this comity exists only to the extent that the particular court deciding the case sees fit to extend it. Accordingly, in some flagrant cases, the members are held liable as partners, the corporate character being disregarded, while in other cases the corporation is recognized and upheld. The latter class of decisions are the

¹ See Chapter XIII.

stronger, and certainly more to be commended and followed. Hence a transferee of stock may find that he has purchased an interest, not in a corporation, but in a partnership. If such be the case, however, he is not liable for all precedent debts of the concern, but only for those incurred subsequently to the registry of his transfer.

§ 425. *Danger of corporate lien.*¹—Frequently corporations are given by charter or statute a lien on a stockholder's stock for debts due from him to the corporation. When such lien exists, a purchaser of the certificate in open market buys subject to the risk that the one from whom he buys owes the corporation a debt, and that the corporation will not allow the transferee of the certificate to obtain a registry until such debt is paid. In many of the States the lien of the corporation cannot be created by by-law. Generally it exists by reason of a provision of the charter. When it does legally exist, it extends to all debts owed by the last registered stockholder, whether the debt be due or not due, and includes uncalled parts of the subscription price of the stock. It does not, however, apply to debts due from one who has bought and sold the certificate without appearing on the registry as a stockholder. The corporation may waive the lien, and a registry without insisting on the lien is such a waiver. The lien of the corporation extends to debts incurred by the transferor after the transfer but before the corporation is notified thereof.

§ 426. *Overissued stock.*²—The capital stock of a corporation is fixed by statute. There is no power in the corporation itself to increase that amount. It can be done only by a legislative enactment. Accordingly, if the corporation issues certificates of stock when the whole capital stock has already been issued, the new issue, if an equivalent amount of outstanding certificates are not surrendered, is an overissue, and is void. Any issue of stock in excess of the amount of the capital stock as fixed by the charter is null and void. The purchaser of such certificates, however, is not without his remedy. His certificate is so much waste paper, and he is not a stockholder, but he may sue the corporation for damages, and recover to the extent of his injury. The purchaser may also sue the corporate officers who participated in the issue

¹ See Chapter XXXI.

² See Chapter XVII.

of the spurious stock, and may recover damages. He cannot, however, hold an innocent transferrer liable. The latter, if he knew nothing of the overissue, is not to be held as a guarantor of the validity of the stock which he sells.

§ 427. *Danger that transferrer or previous holder is an infant, married woman, or lunatic.*¹—A purchase of stock from an infant is a dangerous investment. When the infant comes of age, he may elect to disaffirm, and may hold the transferee liable for the stock. There is less danger, however, in accepting a transfer of stock from an infant who has previously purchased the stock which he sells. This previous purchase, and also his sale of the stock, are technically voidable acts, but after the stock has passed from his control, the law disregards the doubtful medium of title, and considers the purchaser from the infant as the legal stockholder. As regards married women, the old common law allowed the husband to sell her stock after he had reduced it to possession by registering it in his own name on the corporate books. In modern times, however, the right of a married woman to hold and convey personal property, as though unmarried, has been established in most States by statute. Her right to sell shares of stock owned by herself exists where she may sell other personal property similarly owned, and this right depends upon the law and statutes of her domicile. A purchase of stock from a lunatic is void.

§ 428. *Purchase of stock by or from a corporation.*²—In England a corporation cannot purchase shares of its own capital stock. In this country a contrary rule prevails. The statutes governing the corporation, however, sometimes prohibit such purchases. Such is the case with the national banks, and in New York with railroad and banking corporations. In any case, however, whether the corporation purchased the stock legally or illegally, a purchaser of the same stock from the corporation itself is not affected by the invalidity of the title of the corporation. Again, it is a general rule, both in England and America, that one corporation has no right to purchase stock in another corporation. Sometimes the statutes allow such purchases, but more

¹ See §§ 63, 250, 318, 319, 62, 308, 320.

² See Chapter XIX.

often expressly provide to the contrary by prohibiting them. In New York, railroad corporations and manufacturing companies, with a few exceptions for the latter, are restricted herein by such statutes. Nevertheless, whatever rule applies to a purchase by a corporation of stock in another corporation, the law is very clear that a purchaser of such stock from the corporation is protected in his purchase. The unauthorized act of the corporation in purchasing has no effect upon the legality of its sale of the stock.

§ 429. *Purchase from joint owners, partners, and agents.*¹—

One joint owner cannot sell stock standing in the name of two or more as joint owners. One partner may sell and convey stock standing in the partnership name, but not, it seems, where the stock stands in the joint and individual names of all the partners. As regards purchases of stock from agents, greater difficulty occurs. If the purchaser does not know that the vendor is selling as an agent, but supposes he is buying stock owned by the person with whom he is dealing, the purchaser is always protected. The same rule, after considerable doubt and discussion, has been established, even though the purchaser knows that the agent is selling as agent. The sale is valid, and the purchaser is protected provided he has no reason to suspect that the agent is selling in fraud of the owner's rights or in contradiction of his orders.

§ 430. *Purchase of stock at sheriff's execution sale, or from assignee in bankruptcy, or for benefit of creditors.*²—A purchase of stock at an execution sale by the sheriff, is a dangerous investment. Almost always the judgment debtor has already sold and transferred his certificates of stock to a *bona fide* purchaser. If such *bona fide* purchaser has registered the transfer on the corporate books, before the attachment or execution is levied, the purchaser at the execution sale gets nothing. If no such registry has been made, but the judgment debtor sold and transferred the certificate before the levy of attachment or execution, in most of the States, including New York, such a purchaser takes title and the execution purchaser none. In Connecticut, New Hampshire, and a few other States, a contrary rule prevails. If, however, the judgment debtor sells the cer-

¹ See Chapter XIX.

² See Chapter XXVI.

tificate after the attachment or execution is levied, the purchaser takes no title. The execution purchaser is entitled to the stock. A purchaser of stock from an assignee in bankruptcy or insolvency, or for the benefit of creditors, takes a good title if he obtains the certificates of stock. If, however, the insolvent has sold such certificates to another, the latter is entitled to the stock.

§ 431. *Purchase from a pledgee.*¹—A pledgee of stock has no right to sell or repledge the stock held as collateral by him, unless the pledgor intended that he should do so. If, however, the pledgee sells or repledges the stock to one who takes it in good faith, for value, and without notice of the fact that he is dealing with a pledgee of the stock, such a *bona fide* purchaser is protected. He is protected absolutely, and can keep the stock, if he purchased it. If, however, he merely took it in pledge from the pledgee, he is obliged to give up the stock to the real owner, where the latter tenders to the repledgee the amount of the debt owed by the pledgee to the repledgee, for which the stock was given as security. Where, however, a person buys or takes in pledge stock from one who makes known the fact that he is holding the stock as pledgee, the former is not a *bona fide* purchaser. Moreover, he is not a *bona fide* holder where he would not be a *bona fide* holder of a promissory note transferred under similar circumstances, as for instance, where he loans the money at an usurious rate of interest; or where he knows that the person with whom he is dealing is but an agent, and is pledging his principal's stock. In all these cases, where the purchaser or pledgee of stock is not a *bona fide* holder, the real owner and original pledgor of the stock may reclaim his stock from the repledgee, or purchaser from the pledgee, where the original pledgor could recover it from the first pledgee. The repledgee or purchaser from the pledgee stands in the shoes of the first pledgee and has no better rights than the latter.

§ 432. *Pledgee is protected in the same way as purchaser of stock.*¹—The rule contained in this chapter explains the rights, dangers, and liabilities incurred by the purchase of stock. The same rules prevail for the most part in favor of one who receives stock

¹ See Chapters XIX, XXVI.

in pledge. A purchaser and a pledgee are treated in the cases as being similarly protected or similarly not protected. There is, however, one important exception to this rule. If a person who is about to take stock from another, knows that the latter is disposing of the stock as an agent, the former may purchase the stock and be protected, but cannot take it in pledge and be similarly protected. An agent to sell is not an agent to pledge. Another exception to the similarity of position of a vendee and pledgee of stock is that by statute frequently the latter is not liable on stock where the former is liable.

§ 433. *Danger of purchasing from an executor, administrator, or guardian.*¹—There is practically little danger incurred in purchasing stock from any one of these. It is the duty and right of the executors or administrators to sell the personal property and convert it into money. As regards guardians they have the right to change the funds from one investment to another unless a statute prescribes otherwise. Accordingly a purchaser of stock from any one of those is protected in his purchase, even though he knows that his vendor is selling in his official capacity. If, however, the vendee knows that a breach of trust is involved or contemplated, he is not a *bona fide* purchaser and is not protected. All the executors or administrators need not join in a sale of the stock owned by the estate. A sale and transfer by one is sufficient.

434. *Purchase from a trustee.*¹—An entirely different rule prevails as regards stock held by a trustee as trustee. A purchaser of stock which he knows the vendor holds as belonging to a trust estate is bound to ascertain whether by the instrument creating the trust the trustee has a power to sell. If he has no such power, and the vendee knows that he is buying trust estate stock the latter is not protected, but is a party to any breach of trust that may be involved by the sale. If, however, the purchaser has no notice or knowledge that his vendor is selling trust stock, the former is a *bona fide* purchaser to that extent. He is not bound to know that the stock is trust estate stock and consequently is protected in his purchase. Any facts that would put an ordinary intelligent man on his inquiry as to whether the

¹ See Chapter XIX.

stock belongs to a trust estate is notice and prevents the purchaser from claiming to be a *bona fide* purchaser. Thus, such a notice is held to be given by the fact that on the face of the certificate of stock, and following the name of the stockholder, the word "trustee" or equivalent words are written. In California, however, the mere word "trustee" conveys no notice.

435. Sale by vendor to another purchaser without delivery of certificate of stock.¹—A purchaser of certificates of stock has no reason to fear that the vendor can sell the stock to another person without a delivery of the old certificates, and thereby defeat the rights of the purchaser with the certificates. If the purchaser, without certificates, does not obtain registry on the corporate books, he obtains nothing as against the purchaser with the certificates, even though the latter's transaction was subsequent in time to the former. If, however, the former obtains registry on the corporate books, the corporation is at fault, and is liable to the purchaser with the certificates. The corporation must either issue new certificates to the latter or pay damages.

436. Danger of forgery.¹—Forgery cannot be the source of a good title to any chose in action, whether a promissory note, bond and mortgage, or a certificate of stock. Consequently a purchaser of stock takes the risk that some previous owner of the stock, whose name appears on the certificate, either as the registered owner or as transferee, was deprived of his title by forgery. If the forgery has been made, the purchaser cannot claim or hold the stock, although he had no actual knowledge of the forgery. He, however, has recourse to his vendor and may compel him to repay the amount paid for the stock. Where, however, the forgery was committed prior to the last *registered* transfer of that stock a *bona fide* purchaser from or subsequent to the last *registered* holder of that stock is protected. All rights and equities to particular shares of stock are cut off by a registry and sale of the new certificates. The party whose name was forged has recourse then only to the corporation, or to the party obtaining registry, or to previous holders. This limitation to the dangers incident to the purchase of stock extends to other rights and wrongs, as

¹ See Chapter XXI.

well as to a case of forgery, and is of great importance in protecting a *bona fide* purchaser of stock.

§ 437. *Loss or theft of certificates indorsed in blank.*¹—It is extremely doubtful whether a purchaser of a certificate of stock which was indorsed in blank, and which has been lost by the owner and found by another who sells it, or which has been stolen by the latter, would be protected in his purchase, even though he buys in good faith. In a case of negotiable paper, such a purchaser would, of course, be protected. But probably the purchaser of the certificate of stock would not be. No case holds that he would be protected, while many hold that he would not. If the real owner was guilty of gross negligence, perhaps the purchaser from the thief or finder of the certificate indorsed in blank would be protected. In one case this question of negligence was submitted to the jury. Again, sometimes a person sells stock without delivering the certificate, the vendor telling the vendee that the certificates have been lost. Such a title is very precarious. The purchaser should refuse to buy until new certificates are issued by the corporation to the vendor, an issue which the corporation will make upon a suitable bond of indemnity being given to it by the person who alleges a loss. If the purchaser does not take this precaution, he buys subject to having his title defeated by another purchaser who obtained the certificates which are alleged to have been lost.

§ 438. *Danger that a previous holder has been deprived of that same stock by fraud.*²—Shares of stock are the same as other kinds of property, in that a person who has been deprived of his stock by fraud, cannot follow the stock, and take it from the hands of a *bona fide* purchaser for value. The remedy of the defrauded person is for damages against the person defrauding him, or for a retransfer of the stock, if the latter still holds it, together with an injunction against a transfer by the latter. But if the person obtaining the stock by fraud, sells it, even in violation of an injunction, the *bona fide* purchaser for value and without notice is protected. The defrauded party may, however, sue the person defrauding him, in the State of the corporation, and, by an attachment or execution, obtain the stock. Such a

¹ See Chapter XXI.

² See Chapter XX.

danger, however, is the ordinary danger of an attachment or execution. A *lis pendens* of a suit involving stock, never charges the vendor of the stock with notice, as is the case of a *lis pendens* affecting real estate. Cases of fraud in the sale of stock frequently arise in cases of sales by agents, and an appropriation of the proceeds; also when fraudulent representations are made to the vendor.

§ 439. *Statute of frauds.*¹—The Statute of Frauds requires that sales of personal property, exceeding in value a certain amount, generally fifty dollars, shall be valid and enforceable only when the property is partly or wholly delivered, or partly or wholly paid for at the time of the sale, or the terms of the sale are reduced to writing. A sale of stock must conform to this statute. Generally the sale is made by a delivery of the certificate indorsed in blank. Such a sale is legal, and is not void by the Statute of Frauds. The statute applies both to sales of stock which are considered as completed, and also to sales which are to be completed in the future.

§ 440. *Gambling sales of stock.*—A gambling sale or contract to sell stock is void absolutely, and cannot be enforced. As a matter of practical experience, however, it is difficult to prove that a stock sale is a gambling sale. It is such only when both the vendor and vendee intend, not to actually have a delivery of the stock, but to wait and see whether the stock raises or falls in the market, and then to settle the contract by the loser paying the loss. An intent by one of the parties that there shall be no delivery, will not make the sale a gambling one. It must be the intent of both.

§ 441. *Method of assigning a certificate of stock.*²—A certificate of stock is generally assigned by the owners signing the blank transfer, and power of attorney on the back of the certificate. The transfer gives title to him whose name is filled into the blank transfer thus signed. The blank power of attorney is for an entirely different purpose. It enables the person whose name is filled in, to register the transferee as a stockholder in the corporate books. Generally, the power of attorney is filled in with the name of a clerk or agent of the transferee, or a clerk of

¹ See Chapter XX.

² See Chapter XXII.

the corporation who has charge of the registry books. After the registered holder has signed the transfer, leaving the transferee's name in blank, the certificate passes from hand to hand, until some holder cares to fill his name into the blank. He may then obtain registry, or he may execute another transfer and sell the certificate. Transfers need not be under seal in this country. In England, by statute, they generally are required so to be.

§ 442. *Registry of transfer*.¹—A registry of transfer is made by surrendering an old certificate of stock to the corporation, making an entry of the transfer on the corporate registry, and taking from the corporation a new certificate, issued in the name of the transferee. The entry is generally made by a corporate officer, but he may insist on its being made by the person applying for transfer. The object of obtaining the registry is to obtain a right to vote, to receive dividends, and various other incidental stockholders' rights; also to cut off corporate liens and the rights of third parties who may attach or claim the stock. If there is a reasonable legal doubt as to the right of the applicant to obtain registry, the corporation may refuse it, and thus obtain the protection of being compelled to make it by legal proceedings. If two parties claim the stock, each denying the right of the other, the corporation may interplead, provided there is a reasonable legal doubt as to who is entitled to the stock. If the corporation improperly refuses to register a transfer when requested, the applicant may have his remedy in damages, but in most States cannot have a *mandamus*.

§ 443. *Purchaser not affected by rights of holders of that stock back of the last registry*.²—This rule is peculiar to stock certificates, and cuts off rights, even such as those of an owner who has been deprived of the stock by forgery. In this respect certificates of stock are more negotiable than negotiable paper itself. The person who obtains registry first, after the illegal act has been done, is not protected by this rule. But his *bona fide* purchaser of the new certificates and all subsequent purchasers are protected, and cannot be compelled to give up the stock to the prior owner, who was deprived of it illegally.

¹ See Chapter XXII.

² See §§ 367, 369.

§ 444. *Summary.*—It will be seen by a review of the sections of this chapter, that the dangers of loss incurred by the purchase of a certificate of stock are not serious or numerous, and it is well that such is the result. Perhaps the most striking industrial feature of modern times is the accumulation of personal property, and the investment of that property, not in landed estates, but in the stocks and bonds of corporations. Such investments are made, not alone by capitalists, but by thousands whose savings have no other satisfactory mode of disposition. The constant tendency of the statutes, and the decisions of the courts to protect *bona fide* purchasers of certificates of stock, is to be commended and aided. Beyond all question, the surplus wealth of the future will be invested in corporate bonds and stocks. It is well, then, in these days of the formative period of the law governing stock, that the principles governing the transfer of certificates should be formed for the protection and security of an investing public, against secret liens, attachments, claims, and negligence of both the corporation and third persons.

PART III.

MISCELLANEOUS INCIDENTS OF STOCK.

CHAPTER XXV.

STOCK-BROKERS AND THEIR CONTRACTS.

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| <p>§ 445. Definitions.
446. Incompetency, or want of authority of customer.
447. Facts making person a broker or customer unintentionally.
448. Broker must obey specific orders of customer.
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450. Cannot purchase from or sell to himself.
451. Duties and liabilities of customer towards broker.
452. Duties and liabilities of a broker towards customer.
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455. Privity of contract between the opposite customers.
456. Intervening sub-brokers and sub-customers.
457. Purchases or sales on margins—broker as a pledgee.
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§ 445. *Definitions.*—By far the greater part of purchases and sales of stock are made, both in this country and in England, through organizations specially formed for that purpose and called Stock Exchanges. A Stock Exchange is a place of business where those, who make up the membership of the exchange, buy and sell stocks and bonds. These persons are called stock-brokers. A stock-broker is one who buys and sells stock as the agent of another, the latter being called a customer of the stock-broker.¹ Accordingly in an ordinary purchase of stock through stock-brokers, there are, generally, at least four persons involved—the two brokers and their respective customers. Stock-brokers have

¹ In *Sibbald v. The Bethlehem Iron Company*, 83 N. Y. 378 (1881), Finch, J., favors the definition from *Pott v. Turner*, 6 Bing. 702, 706, where a broker is defined as "one who makes a bargain for another and receives a commission for so doing." Story on Agency, § 28 (9th ed.),

says: "The true definition of a broker seems to be that he is an agent employed to make bargains and contracts between other persons in matters of trade, commerce, or navigation, for a compensation commonly called brokerage."

a language of their own. They have coined and put into general circulation certain phrases and terms descriptive of their business. These terms have become so closely identified with the subject of stock and transactions in stock that the courts have defined their meaning and explained their application.¹

§ 446. *Incompetency, or want of authority of customer.*—

Any person may be a stock-broker who may make a contract, but it is beyond the power of a national bank to act as a broker.² Strict rules prevail as to who may be a customer. An infant is not bound by his contracts with or through a stock-broker any more than he is bound by his other contracts. Moreover, if the broker carries on stock transactions for an infant, he is liable to the latter for all moneys lost thereby.³ Again, a broker who sells or buys

¹ A "bull" is a dealer who endeavors to make the price of stocks go higher. A "bear" is a dealer who endeavors to make the price of stocks go lower. A "short" sale is a sale of stocks which the seller does not possess, but which he expects to purchase later on at a lower figure, thus fulfilling his contract and making profit by the decline. In the meantime the broker generally borrows the stock from other parties to deliver to the vendee, and to be returned to the person loaning the stock at the end of the transaction. The broker is bound to continue the transaction for a reasonable time. The customer deposits with the broker a small amount of money as security, called a margin, and he is bound to keep the margin good. *Hess v. Rau*, 95 N. Y. 359 (1884); *White v. Smith*, 54 N. Y. 522 (1874); *Knowlton v. Fitch*, 52 N. Y. 288 (1873); *Appleman v. Fisher*, 54 Md. 540 (1871); *Sistare v. Best*, 88 N. Y. 527, 533 (1882). A "long" purchase of stock is a purchase in the expectation that the stock will rise in value. Stock options are of three kinds—puts, calls, and straddles. A "put" is a contract whereby a person has the privilege of requiring another person to take from the former certain specified stock at a specified price, at any time within a specified period of time, the former not being bound to sell. See *Bigelow v. Benedict*, 70 N. Y. 202 (1877). A "call" is a contract whereby a person has the privilege of requiring another person to sell or deliver to the former certain specified stock at a specified price, at any time within a certain specified period, the former not being bound to purchase. A

"straddle" or "spread eagle," is a combination of a put and a call. It gives a person the double privilege of delivering to or demanding from another person certain stock at a certain price within a specified time. *Harris v. Tumbridge*, 83 N. Y. 92 (1880); *Story v. Salomon*, 71 N. Y. 420 (1877). A "corner" exists where the "bears" have sold a large quantity of stock "short," and cannot borrow the stock to fill their contracts, but must buy it from those who have cornered the market on that stock. See *Cameron v. Durkheim*, 55 N. Y. 425, 438 (1874). As to the legality of these various transactions, see §§ 341-348. A "stock-jobber" is defined to be a person who keeps "a sort of common book or register where brokers who have shares to sell go to deposit them, and persons who want to buy go to buy them, who finally at the proper time bring together their customers on the one side and the other, so as to procure the result desired by both, each of the parties to the transaction still remaining unknown to the other." *Sheppard v. Murphy*, 16 W. R. 948 (1868). Another definition is that a stock-jobber is a dealer in stocks; one who buys and sells stock on his own account on speculation.

² *First Nat'l Bk. of Allentown v. Hock*, 20 Alb. L. J. 216.

³ *Ruchizky v. De Haven*, 97 Pa. St. 202. The transactions in this case were held to be gambling contracts. *Heath v. Mahoney*, 12 Week. Dig., 404 (1881). The broker himself may be an infant and may repudiate his obligations. See 4 Law Notes, 314.

stock in the name of an infant, is himself liable to the other party, in case the contract is not completed, by reason of such infancy.¹ On the other hand, if the broker's customer hands in the name of a third person, an infant, as the seller or purchaser, such customer is liable to the broker for liabilities thereby incurred by the latter.²

§ 447. *Facts making person a broker or customer unintentionally.*—The relationship of broker and customer may be established and exist, although one of the parties is personally ignorant of such a relationship.³ A broker also may be liable as such, in transactions where he had no intention of incurring any liability.⁴

§ 448. *Broker must obey specific orders of customer.*—A broker is bound to obey and carry out strictly the orders of his customer in the purchase or sale of stock. This rule is rigidly insisted upon by the courts. The orders of the customer may be such as he wishes to give, and when given they must be obeyed, or liability will be incurred by the broker.⁵ When the customer fixes a limit at which the broker may purchase, the latter cannot bind the customer by a purchase at a higher figure.⁶ Frequently the

¹ Nickalls v. Merry, L. R. 7 H. L. 520 (1875); Heritage v. Paine, 34 L. T. 947 (1876); Maxted v. Paine, L. R. 4 Ex. 81 (1869). The first case holds him liable, although ignorant of the infancy of his customer. See same case, Merry v. Nickalls, 41 L. J. (Ch.) 767 (1872). Broker is liable, although the name of the infant was passed to him by another broker. Dent v. Nickalls, 29 L. T. 536 (1873). It is no defense to the broker that the infant's father was the real customer. Nickalls v. Eaton, 23 L. T. 689 (1871).

² Peppercorne v. Clinch, 26 L. T. 656 (1872).

³ Thus the customer may be bound by the acts of his clerk. Webb v. Challoner, 2 F. & F. 120 (1860). So also where the firm does a broker business through its agents, the transactions by the agents on their own private accounts, but ostensibly for the firm, will bind the firm. Wells, Fargo & Co. v. Welter, 15 Nev. 276 (1880).

⁴ As where he continues to allow his name to remain in the firm name after its dissolution. Hixon v. Pixley, 15 Nev. 475 (1880). Also, where one of the firm

is a trustee and defaults therein, the firm having charge of the trust estate's stocks. De Ribeyre v. Barclay, 23 Beav. 107 (1856). As a silent partner he cannot prevent a customer from setting off against a liability a debt personal to the ostensibly sole broker. Read v. Jaudon, 35 How. Pr. 303 (1868).

⁵ Parsons v. Martin, 77 Mass. 111 (1858). Thus, where the customer authorizes a sale if the stock goes down to 51, but the broker sells when it goes down to 52, he is liable for an unauthorized sale. Clarke v. Meigs, 10 Bosw. 337 (1863). Cf. Whelan v. Lynch, 60 N. Y. 469 (1875); Jones v. Marks, 40 Ill. 313 (1866). But the broker may correct a palpable error in the order given him by his customer. Luffman v. Hay, 13 N. Y. Week. Dig. 324 (1881).

⁶ Whether a limit was fixed is a question for the jury, if the facts are disputed. Cf. Smith v. Bouvier, 70 Pa. St. 375 (1872). The customer may ratify the unauthorized purchase. Genin v. Isaacson, 6 N. Y. Leg. Obs. 213 (1848). If the power to sell depends on the construction of writings, it is a question of

customer gives to the broker a "stop order," which is an order to sell or buy, as the case may be, at a certain specified figure, or upon a specified contingency. Under this order the broker must sell or buy when the price or contingency occurs, but not *until* it occurs. If the market changes too quickly for him, he must sell or buy at the market price immediately after the fixed price or contingency arises.¹ The customer may leave it in the discretion of the broker as to the best time for buying or selling.³ When this is done the broker must exercise such discretion in good faith and with reasonably good judgment and care.³

§ 449. *Must act in good faith and in reasonable time.*—The broker must make the purchase or sale in good faith on the best terms possible, and must give the customer the advantage of the transaction as actually made. Any material failure to do this, or to make the sale or purchase as directed, will release the customer from the transaction, although it was reported to him as made in accordance with orders.⁴ The broker is allowed a reasonable time within which to make the sale or purchase.⁵

law only. *Davis v. Gwynne*, 57 N. Y. 676 (1874); s. c., 4 Daly, 218 (1871). But the written order may be subsequently modified by parol, *Burkitt v. Taylor*, 86 N. Y. 618 (1881); *Clarke v. Meigs*, 10 Bosw. 337 (1863); or be waived. *Hope v. Lawrence*, 50 Barb. 258 (1867).

¹ *Porter v. Wormser*, 94 N. Y. 431 (1884); *Bertram v. Godfrey*, 1 Knapp's Rep. P. C. 381 (1830). The latter case involved an absolute order to sell should the stock reach a certain price.

² Such discretion when given is revoked only by clear notice of revocation. *Davis v. Gwynne*, 4 Daly, 218 (1871).

³ *Harris v. Tumbidge*, 83 N. Y. 92 (1880).

⁴ Where the broker buys in his own name at a price less than the price reported to the customer, sells without notice, and subsequently pretends to sell again, the whole transaction is void as to the customer. *Levy v. Loeb*, 85 N. Y. 365 (1881); 89 Id. 386. So, likewise, where he purchases an option, instead of cash purchase, and reports a higher price than that paid. *Voris v. McCready*, 16 How. Pr. 87 (1856). So, likewise, where the broker varies the order from a cash purchase to an option, he himself taking

the risk of the option. *Dey v. Holmes*, 103 Mass. 306; *Pickering v. Demeritt*, 100 Mass. 416 (1868).

⁵ *Fletcher v. Marshall*, 15 Mees. & W. 755 (1846). Cf. *Dickinson v. Lilwal*, 1 Starkie, 128 (1815), which holds that the transaction must be carried out on the day of the order. The broker is entitled to his commission, although his customer fails before the transaction is made. *Inchbald v. The Western Coffee Co.*, 43 L. J. (C. P.) 15. The contract is to be carried out within a reasonable time. A broker's custom is evidence as to what is reasonable time. *Stewart v. Cauty*, 8 Mees. & W. 160 (1840). A few hours notice held insufficient. *Johnson v. Mulvy*, 51 N. Y. 634 (1872). "Usually the broker is entitled to a fair and reasonable opportunity to perform his obligation, subject of course to the right of the seller to sell independently. But that having been granted him, the right of the principal to terminate his authority is absolute and unrestricted, except only that he may not do it in bad faith and as a mere device to escape the payment of the broker's commissions." *Sibbald v. The Bethlehem Iron Co.*, 83 N. Y. 378, 384 (1881).

§ 450. *Cannot purchase from or sell to himself.*—A broker cannot, in behalf of his customer, buy or sell, with himself as the other principal. The law will not allow him to act both as agent and as principal at the same time. Such an act is a constructive fraud, on account of his fiduciary relation, and will be set aside.¹ Custom or usage cannot legalize such a transaction.² The broker may, however, show by parol evidence that he did not deal with himself, though writings indicate otherwise.³ And there is no rule which prevents the broker from acting as agent both for the selling and the buying customer.⁴

§ 451. *Duties and liabilities of customer towards broker.*—A stock-broker is but the agent of his customer. As such he may bind his customer by acts within the scope of his authority, and compel the customer to respond to the liability. Thus the broker may proceed to close the transaction, paying out his own money as though it was his own business, and may then compel the customer to repay to him the money so expended in the customer's behalf.⁵ Or if his customer refuses to carry out the transaction, the broker may settle with the opposite party by paying the loss incurred by buying or selling the stock elsewhere, and may then sue his customer for the differences thus paid.⁶

¹ Conkey v. Bond, 36 N. Y. 427; Brookman v. Rothschild, 3 Sim. 153 (1829); Marye v. Strouse, 5 Fed. Rep. 483 (1880); Robinson v. Mollett, L. R. 7 H. L. 802, 818, 826 (1874). Even though the purchase was in good faith and at a lower figure than the market price. Tausig v. Hart, 58 N. Y. 425 (1874); Gillett v. Peppercombe, 3 Beav. 78 (1840). In Bryan v. Baldwin, 53 N. Y. 232 (1873), the court says: "The plaintiff being pledgee of the stock, and in that character exposing it for sale, could not become the purchaser unless the defendant assented to such purchase. Story on Bailments, § 319; Torry v. Bk. of Orleans, 7 Paige, 649; Hawley v. Cramer, 4 Cow. 736. This sale to the plaintiff was not void but voidable at the election of the defendant. Edwards on Bailments, 260. The defendant was at liberty to ratify the sale, and had he done so it would have been valid for all purposes. The ratification would have made it lawful, and relieved it from any imputation of being tortious as to him. . . . But

the defendant has not done this, but has elected to treat the purchase by the plaintiff as illegal. This avoids the sale, and that being avoided by the defendant, the parties are remitted to their rights the same as though no sale had been attempted."

² Commonwealth v. Cooper, 130 Mass. 285 (1881). The custom of brokers to buy in large quantities and sell in small quantities is illegal. Robinson v. Mollett, L. R. 7 H. L. 802 (1874).

³ Porter v. Wormser, 94 N. Y. 431 (1884).

⁴ Knowlton v. Fitch, 52 N. Y. 288 (1873).

⁵ Bayley v. Wilkins, 7 C. B. 886 (1849); Whitehouse v. Moore, 13 Abb. Pr. 142 (1861); Dails v. Lloyd, 12 C. B. 531. Cf. *Ex parte Neilson*, 3 De G., M. & G. 556 (1853).

⁶ Durant v. Burt, 98 Mass. 161 (1867); Bayliffe v. Butterworth, 5 Railw. Cas. 283, per Parke, B.; Marten v. Gibbon, 33 L. T. 561 (1876); Biederman v. Stone, L. R. 2 C. P. 504 (1867).

He may also recover his disbursements, commissions, and interest.¹ The customer is liable to the broker for stock purchased, although the stock turns out to be spurious or unauthorized.² If the broker, however, seeks to recover the full value of the stock, he must first tender the stock to the customer,³ or he must sell it after due notice to the customer, and thus accurately ascertain the loss.⁴ If he is seeking to recover for differences paid the opposite broker in settlement, *assumpsit* is his remedy.⁵ He must clearly prove that the customer authorized the order.⁶

§ 452. Duties and liabilities of a broker towards customer.

—The broker also owes certain duties and incurs certain liabilities in his relations towards his customer. It is said that he cannot sell on credit, since that is not the usual course of his business.⁷ He is liable in damages for failure to buy or sell in accordance with his express orders.⁸ Where the customer fails to carry out the transaction, but the broker does carry it out at a profit, the profit belongs to the customer.⁹ But the customer is

¹ Where the commissions and interest were paid to other brokers, it may be charged to the customer. *Robinson v. Norris*, 51 How. Pr. 442 (1874). Even though that interest be usurious. *Smith v. Heath*, 4 Daly, 123 (1871). On commissions, see *Inchbald v. Western Coffee Co.*, 43 L. J. (C. P.) 15. Excessive expenses will not be allowed, although customary. *Marye v. Strouse*, 5 Fed. Rep. 483 (1880). But the broker is entitled to commissions only when he has rendered some service to the customer. *Sibbald v. The Bethlehem Iron Co.*, 83 N. Y. 378 (1881); *Hoffman v. Livingston*, 46 N. Y. Super. Ct. 552 (1880). The case, *Hatch v. Douglas*, 48 Conn. 116 (1880), holds that the broker's customary monthly charges and interest thereon are not usurious. Cf. *Robinson v. Norris*, 6 Hun, 233 (1875).

² See *Adamson v. Jarvis*, 4 Bing. 66 (1827). Spurious stock. See *Peckham v. Ketcham*, 5 Bosw. 506 (1859). So also for spurious stock innocently given to the broker to sell. *Westropp v. Solomon*, 8 C. B. 345 (1849).

³ *Merwin v. Hamilton*, 6 Duer, 244 (1856); *Bowlby v. Bell*, 3 Com. B. 284 (1846). But after once tendering it, he need not continually keep it on hand. *Wynkoop v. Seal*, 64 Pa. St. 361 (1870).

⁴ *Monroe v. Peck*, 3 Daly, 128 (1869). In *Rosenstock v. Tormey*, 32 Md. 169, the necessary allegations were held to be

a purchase of stock according to an order at fair market price, which was paid, and the customer notified, and payment demanded; willingness to deliver the stock; refusal of customer to pay; notice of sale; a proper sale; and loss.

⁵ *Pollock v. Stables*, 12 Q. B. 765 (1848). *Contra*, *Child v. Morley*, 8 Term R. 610 (1800).

⁶ *Ward v. Van Duser*, 2 Hall (N. Y.), 167. In *White v. Baxter*, 71 N. Y. 254 (1877), the court held that a customer's contract with his broker to protect the latter against loss by expulsion from the Stock Exchange for non-compliance with its rules, is a valid and enforceable contract.

⁷ 2 Kent's Com., 622 (b), 12th ed.

⁸ *Speyer v. Colgate*, 4 Hun, 622 (1875); *Whelan v. Lynch*, 60 N. Y. 469 (1875). The case of a wool broker. See also *Jones v. Marks*, 40 Ill. 313 (1866). The damages may sound *in tort*, thus preventing a release in bankruptcy from barring the action. *Parker v. Crol*, 5 Bing. 63 (1828). Under the New York Code he may be arrested if he does not use the money for the purpose designated. *Dubois v. Thompson*, 1 Daly, 309. And in England he is liable criminally. *Regina v. Cronmire*, 54 L. T. Rep. 580 (1885).

⁹ *Fowler v. N. Y. Gold Ex. Bk.*, 67 N. Y. 138 (1876).

not entitled to stock held for him by the broker until he pays the broker all his reasonable disbursements thereon.¹ The broker may deposit a margin with the opposite broker, according to custom, and not be responsible to his customer if it is lost,² although the rule may be otherwise as to a delivery of the stocks themselves.³ The broker is required to exercise reasonable diligence and care, and no more.⁴ The broker has a lien on the customer's property in his hands for all debts due to the former.⁵ But he has no such lien if he knows that the customer is acting as agent for another.⁶ It is a question of doubt whether a broker who has received commissions from a person guilty of embezzlement is liable to pay over to the persons injured by his customer, commissions so received.⁷ A broker may, by bill of discovery, be compelled to disclose acts amounting to misconduct.⁸

§ 453. *Method of completing a broker's contract.*—The formalities and method of completing a stock-broker's contract is governed largely by the usages of the Stock Exchange. It is well established law that when a man sells or buys shares through his broker on the Stock Exchange, he enters into an implied contract to sell or buy according to the custom and usages prevalent in that body.⁹ These usages and customs are to be found, for the most part, in the rules of the Stock Exchange, so far as the formalities of completing the contract are concerned. Occasionally, however, such formalities are reviewed and sanctioned by the courts.¹⁰

¹ See *McEwen v. Woods*, 11 Q. B. 13, where the broker paid calls made on the stock after its sale.

² *Gheen v. Johnson*, 90 Pa. St. 38 (1879).

³ *Brown v. Boorman*, 11 Cl. & F. 1 (1844).

⁴ *Phillips v. Noir*, 59 Ill. 155; *Gheen v. Johnson*, 90 Pa. St. 38 (1879).

⁵ *Jones v. Peppercorne*, 5 Jur. N. S. Pt. 1, p. 140.

⁶ *Fisher v. Brown*, 104 Mass. 259 (1870); *Pearson v. Scott*, L. R. 9 Ch. D. 198 (1878).

⁷ See *Butler v. Finck*, 21 Hun, 210 (1880). The case of *Taft v. Chapman*, 50 N. Y. 445 (1872), seems to hold that the broker is not liable where he acted without knowledge of his customer's acts. See also s. c. under name *Brownson v.*

Chapman, 63 N. Y. 625 (1875). See also *Porter v. Parks*, 49 N. Y. 564 (1872).

⁸ *Green v. Weaver*, 1 Sim. 404 (1827). See *Raulings v. Hall*, 1 Carr. & P. 11 (1823).

⁹ See § 462.

¹⁰ Thus a usage by which the ultimate purchaser's name is handed to the seller, for the purpose of having the latter execute a transfer to the former, is upheld. *Sheppard v. Murphy*, 16 W. R. 948 (1868). The custom of giving the seller time to investigate and object to a purchaser may be insisted on by the seller. *Sumner v. Stewart*, 69 Pa. St. 321 (1871). The purchaser may be compelled, by a bill in equity, to register the transfer made through brokers. *Paine v. Hutchinson*, L. R. 3 Eq. Cas. 257 (1866).

§ 454. *Privity of contract between broker and opposite parties.*—A broker who buys or sells stock does so subject to certain liabilities towards the parties to whom he sells or from whom he buys. If he does not send in the name of his customer, he is liable on the transaction as though he were the principal himself.¹ He has been held liable for a forgery perpetrated by his customer.² Where, however, the broker hands in the name of his customer, and that name is accepted, the broker is thereby discharged,³ unless, of course, the name is unauthorized, or is that of an infant.⁴ Upon the disclosure by the broker of his customer's name, the opposite party has the option of holding either the broker or his customer responsible, but cannot hold both.⁵

§ 455. *Privity of contract between the opposite customers.*—When the broker of one customer has agreed with the broker of another customer on the terms of a purchase and sale of stock, there immediately arises a privity of contract between the two customers. The purchasing customer is liable to the selling customer for all calls and liabilities arising on the stock after the broker's contract is made, if the selling customer is obliged to pay such liabilities by reason of his being the registered stockholder.⁶ So also the purchasing customer may hold the selling customer responsible for the carrying out of the contract.⁷ It has been

¹ Wynne v. Price, 3 De G. & Sm. 310 (1849).

² Royal Exchange Ins. Co. v. Moore, 11 Week. Rep. 592. The broker herein sold in his own name, but the opposite party knew he acted as a broker.

³ Maxted v. Paine (2d action), L. R. 6 Ex. 132 (1871), holding that the broker does not guarantee his customer's responsibility, nor that he is the real purchaser. So also of the stock-jobber. Grissell v. Bristowe, L. R. 4 C. P. 36 (1868). *Contra*, Cruse v. Paine, 37 L. J. (Ch.) 711.

⁴ See § 446. Broker handing in the name of a customer without authority is himself liable. Maxted v. Norris, 21 L. T. 535. *Cf.* Shepherd v. Gillespie, L. R. 5 Eq. Cas. 293 (1867).

⁵ Watson v. Miller, 11 Week. Notes, 18 (1876). A custom or usage releasing the broker from this liability is void. Magee v. Atkinson, 2 Mees. & W. 440 (1837). *Cf.* Jones v. Littledale, 1 Nev. & Per. 677 (1837), the sale being of hemp. Also Thomson v. Davenport, 9 Barn. & Cr. 78 (1829), holding that the purchaser's

option remains open until the name of the undisclosed principal is given. It is for the jury to say which one the opposite customer gave credit to, irrespective of a Stock Exchange custom. Mortimer v. McCallan, 6 Mees. & W. 58 (1840).

⁶ Hawkins v. Maltby, L. R. Ch. App. 200 (1869); affirming s. c., L. R. 6 Eq. 505. Evans v. Wood, L. R. 5 Eq. Cas. 9 (1867); Hodgkinson v. Kelly, L. R. 6 Eq. Cas. 496 (1868); 37 L. J. (Ch.) 837; Remfrey v. Rutter, 1 Ell. Bl. & Ell. 887 (1858); Allan v. Graves, 39 L. J. 157 (1870). A Stock Exchange custom, making the broker a principal, does not prevent the customer suing as principal. Langton v. Waite, 16 W. R. 508 (1868). Refusal of directors to register the sale does not enable the purchasing customer to recover back the purchase price. Stray v. Russell, 1 El. & El. 888 (1859).

⁷ Even though the selling customer did not authorize the use of his name, but knew of it and did not object. Shepherd v. Gillespie, L. R. 5 Eq. Cas. 293 (1867).

held that the remedy may be an action at law¹ or in equity. The right of set-off for other debts applies as between the two customers,² but not for debts due from one of the brokers to the opposite customer.⁴

§ 456. *Intervening sub-brokers and sub-customers.*—Where a customer's broker employs another broker to transact the business, the customer cannot compel the second broker to complete the contract as he might compel the first broker.⁵ The second broker cannot claim a lien on the stock for debts due him from the first broker.⁶ If the first broker merely introduces the parties, he cannot charge a commission therefor, although custom allows it.⁷ The real customer may hold an intermediate customer liable.

§ 457. *Purchases or sales on margins—Broker as a pledgee.*—By far the larger part of a stock-broker's business consists of purchases and sales of stock on what is called a "margin."⁸ The customer deposits with the broker, as security, a sum of money, equal to but a small part of the value of the stock involved. This sum of money is the "margin." If the customer's order is to purchase, then the broker keeps both the margin and the purchased stock as security against loss in the final closing of the transaction. If the customer's order is to sell, then the broker sells, but having no stock to deliver he borrows the same from other parties, and delivers it to the purchaser, the broker still keeping the margin as security. Frequently no stock passes, nor is intended to pass, but merely the ultimate profit or loss called "differences" is paid; the losing customer loses the whole or part of his margin, the winning customer getting back his margin and also the profits, less commissions. This is a gambling contract, and

¹ *Street v. Morgan*, L. R. 4 Ex. 384. See also *Davis v. Haycock*, L. R. 4 Ex. 373 (1869).

² *Sheppard v. Murphy*, 16 W. R. 948 (1868).

³ *Carr v. Hinchliff*, 4 Barn. & Cr. 547 (1825).

⁴ *Fish v. Kempton*, 7 C. B. 687 (1849). See also *Sweeting v. Pearce*, 7 C. B. N. S. 449 (1859). Unless, possibly, where the customer supposed the opposite broker was the principal. See *Kelley v. Munson*, 7 Mass. 318 (1811).

⁵ *Booth v. Fielding*, 1 Week. Notes, 245 (1866).

⁶ *Fisher v. Brown*, 104 Mass. 259 (1870).

⁷ *Gibson v. Crick*, 1 Hurl. & C. 142 (1862). He may hold the intermediate customer or agent liable for set-off due from the latter to the broker. *Jaycox v. Cameron*, 49 N. Y. 645 (1872).

⁸ A margin "means, in the broker's lexicon, additional collateral security against loss to the broker, while he is . . . carrying stock for his employer." *McNeil v. Tenth Nat. Bk. of N. Y.*, 55 Barb. 59 (1869).

like all gambling contracts, whether in or out of a stock exchange, is not enforceable.¹ But a purchase or sale of stock on margins, where there is no proof of an intent not to actually deliver the stock, is legal.² The relation between a customer and his broker in cases where the broker buys for his customer and retains the stock as security, is the relation of a pledgor towards a pledgee, the customer being the pledgor, the broker being the pledgee, and the stock being the article pledged.³ Some of the most important questions connected with brokers' contracts arise out of this pledgee relationship. This subject, however, is fully treated in the following chapter. Like an ordinary pledgee of stock, the broker may have the stock transferred into his own name;⁴ he is not allowed to repledge the stock;⁵ and he can put

¹ *McBurney v. Martin*, 6 Conn. 502.

² See Ch. XX, where the character, effect, and non-enforceability of a broker's gambling contracts are fully treated. A "margin" transaction is not necessarily gambling and invalid. The important case of *Hatch v. Douglas*, 48 Conn. 116 (1880), clearly sets out the legality of such contracts. The court said: "It is pretty evident that the parties did not contemplate that the stock should be actually transferred to the defendant. . . . The defendant [customer], through his agents, the plaintiffs, actually purchased the stock, and there was an actual delivery—not to the principal, but to the agents for the principal." The brokers knew "that the defendant was speculating, and that they advanced him money for that purpose. But that was neither illegal nor immoral. . . . No case has been decided which declares such a contract illegal. If we should so hold, it would be difficult if not impossible to draw the line between legal and illegal transactions."

³ *Markham v. Jaudon*, 41 N. Y. 235 (1869); *Baker v. Drake*, 66 N. Y. 518 (1876). The broker is bound to keep constantly on hand the amount of stock so held on margin, *i. e.* pledged. *Taussig v. Hart*, 58 N. Y. 425 (1874). In fact, the broker is obliged to conform to the rules governing pledgees of stock, a subject treated in Ch. XXVI. The customer as pledgor may claim his stock from the broker's assignee for the benefit of creditors if the customer can identify it. *Chamberlain v. Greenleaf*, 4 Abb. N. C. 178 (1878); see *Boylan v. Huguet*, 8 Me. 345 (1873).

⁴ *Horton v. Morgan*, 19 N. Y. 170.

⁵ *Dykers v. Allen*, 7 Hill, 497, where it was understood between a firm of brokers and its customers, for whom, and on whose order, it bought stocks on the security of a margin, that the firm might, according to the usual course of business, pledge or hypothecate as security for loans to the firm the stocks thus bought, held that a mere pledge of such stocks would not be of itself a conversion. *Chamberlain v. Greenleaf*, 4 Abb. N. C. 178 (1878); see also *Lawrence v. Maxwell*, 58 Barb. 511; 6 Lans. 469; 53 N. Y. 19. In *Wood v. Hayes*, 15 Gray, 375, it was held that "a broker who advanced money to buy stock for another, and held it in his own name, might, so long as he had not been paid or tendered the amount of his advances, pledge it as security for his own debt to a third person, without making himself liable to an action by his employer, and this upon the ground that the contract was conditional to deliver the shares upon the payment of the money." Approved in *Covell v. Loud*, 135 Mass. 41 (1883), where it was held that where the customer was unable to advance further margin and tells the broker to do the best he can, he may sell without notice. The decided weight of authority, however, holds that unless the power is expressly given to the broker to repledge the stock, he cannot legally repledge it. See Ch. XXVI. This, however, does not affect the rights of a repledgee or a purchaser of the stock from the broker. A *bona fide* transferee absolutely or in pledge from a broker holding his customer's stock in pledge is protected to

his customer in default only by tendering the stock and demanding payment for their whole value less the margin.¹

§ 458. *Broker's rights and duties on failure of margin.*—When the "margin" which the customer deposits with his broker happens to become exhausted by the fluctuations of the market adversely to the customer, the difficult questions arise as to the several rights and duties of the broker and of the customer. If the broker is under orders to close the transaction when the margin becomes exhausted, he of course is obliged to do so.² But, otherwise, the rule is that the broker cannot summarily close the transaction, even though he has fear of greater loss, involving a loss by himself. He is obliged to demand further margin from his customer, at the same time notifying him that the previous margin is exhausted; also that in case the margin is not made good that he will close the transaction, holding the customer liable for the loss; also stating the time and place of such threatened sale.³ The notice must be given a reasonable time before such closing of the transaction, and notice may be sent by mail.⁴ If the broker fails to comply with these rules, and sells, he is guilty of conversion of the stock.⁵ Where the broker is merely authorized to sell, he is not bound to sell.⁶

§ 459. *What will excuse notice and demand for more margin.*—All these rights of the customer to notice of failure of margin; demand of more margin; notice of intent to sell, and of time and place of sale, may be waived, and brokers generally

the extent of the transfer, the transferee having no notice of the fact that the stock was held in pledge by the broker. *Thompson v. Toland*, 48 Cal. 99 (1874); *McNeil v. Tenth Nat. Bk. of N. Y.* 46 N. Y. 325 (1871); *Zulick v. Markham*, 6 Daly, 129 (1875), and see many cases in § 321. These cases apply equally whether the person transferring contrary to law is an agent or a pledgee, and equally also whether he sells or only repledges.

¹ *Read v. Lambert*, 10 Abb. Pr. N. S. 428 (1871).

² See § 448.

³ *Markham v. Jaudon*, 41 N. Y. 235, overruling *Hanks v. Drake*, 49 Barb. 186 (1867), and *Sterling v. Jaudon*, 48 Barb. 459. See also *Kenfield v. Latham*, 2 Cal. Lg. Rec. 235. *Cf. Worthington v. Tor-*

mey, 34 Md. 182 (1870), and see Ch. XXVI. Leaving notice at office held insufficient where it did not reach the customer. *Bryan v. Baldwin*, 52 N. Y. 232 (1878).

⁴ *Worthington v. Tormey*, 34 Md. 182 (1870). Two days' notice held sufficient. *Stewart v. Drake*, 46 N. Y. 449 (1871).

⁵ *Baker v. Drake*, 66 N. Y. 518 (1876). *Cf. Gregory v. Wendall*, 40 Mich. 432 (1879), involving a purchase of Stocks alone, in brokers' transactions, give rise to the relation of pledgor and pledgee.

⁶ *Robinson v. Norris*, 51 How. Pr. 442 (1874); *Esser v. Linderman*, 71 Pa. St. 76 (1872); *Cf. Harris v. Tumbridge*, 83 N. Y. 92 (1880).

require their customers to sign written contracts to that effect.¹ It is doubtful whether the death of the customer will authorize the broker to close the transaction without notice.² A custom of brokers to dispense with these notices is void, and not binding on the customer.³ The fact that a panic occurs, or unusual fluctuations of the market happens, do not excuse a broker from giving such notice.⁴

§ 460. *Customer's remedies and damages herein.*—For an unauthorized sale by a broker of stock held upon a margin, the customer has ample remedies. He may claim the benefit of the sale or may claim the value of the stock.⁵ Or the customer may require the broker to replace the stock, and upon his failure so to do, the customer may replace it himself and charge the broker with the loss.⁶ Or the customer may recover the advance in the

¹ Thus, a written authority to the brokers "to sell, at their discretion, at public or private sale, without any notice whatever, the stocks or gold which they might be carrying for the plaintiff, whenever the margin should fall below" a certain figure, waives all the customer's rights herein. *Wicks v. Hatch*, 62 N. Y. 535 (1875). See also *Cameron v. Durkheim*, 55 N. Y. 425 (1874). The customer may waive his rights after the broker has made the unauthorized sale. *Stewart v. Drake*, 46 N. Y. 449 (1876); *Milliken v. Dehon*, 27 N. Y. 364 (1863). But authority "to close the account, without notice, by purchase or sale, at public or private sale," does not waive right to notice of failure of margin and demand for more. *Stenton v. Jerome*, 54 N. Y. 480 (1873); *Kenfield v. Latham*, 2 Cal. Leg. Rec. 235. A common form of the contract which the broker requires the customer to sign is the following:

"— hereby agree to maintain with you at all times a margin of — per centum of the par value of all stocks and bonds against which you have made or may hereafter make advances to — and a like margin on stocks or bonds which — have borrowed or may hereafter borrow through you to make deliveries on sales made for — account or otherwise.

"In case — margin should become impaired and the same is not promptly made good in response to personal notice or notice sent by wire or letter and direct-

ed to — usual address, you are authorized in your discretion to buy or sell at the N. Y. Stock Exchange or at public or private sale, without further notice, such securities as may be necessary to place the account in condition satisfactory to you, or to close the same entirely, as you may prefer.

"In case of my decease you are hereby authorized to close my account by purchase or sale of securities as the same may require. —"

² The broker will be protected in continuing the transaction until personal representatives are appointed. *Hess v. Rau*, 35 N. Y. 359 (1884). Cf. *Lacey v. Hill*, L. R., 8 Ch. App. 921 (1873).

³ *Markham v. Jaudon*, 41 N. Y. 235 (1869); *Taylor v. Ketchum*, 35 How. Pr. 289 (1861); s. c. 5 Robt. 507. *Contra*, *Appleman v. Fisher*, 34 Md. 540 (1871), a case of a gold-broker. Also *Colket v. Ellis*, 10 Phil. 375 (1875), where both parties were brokers and knew the custom. If the customs are expressly made a part of the contract, insolvency of the customer authorizes sale without notice, such being the custom. *Lacy v. Hill*, L. R., 18 Eq. 182 (1874).

⁴ *Markham v. Jaudon*, 41 N. Y. 235 (1869); *Brass v. Worth*, 40 Barb. 643 (1863); *Ritter v. Cushman*, 7 Robt. 294 (1867).

⁵ *Taussig v. Hart*, 58 N. Y. 425 (1874).

⁶ *Baker v. Drake*, 53 N. Y. 211, 217 (1873); *Colt v. Owens*, 99 N. Y. 368 (1882).

market price from the time of the sale up to a reasonable time to replace the stock, after notice of the sale.¹ The unauthorized sale by the broker herein is not necessarily a fraudulent sale.² The suit should be at law,³ and demand and tender need not be alleged.⁴

§ 461. *Broker's remedies and damages herein.*—Nevertheless, although the broker makes an unauthorized closing of the transaction, yet he may compel his customer to pay him the loss incurred therein, and the customer may set up, as a counterclaim to the broker's action, the benefits which he would have realized, if the unauthorized act had not occurred.⁵ Where the broker's act is strictly according to law, he is, of course, entitled to recover from his customer any loss that has been sustained in excess of the margin.⁶

§ 462. *Broker's customs and usages.*—It has been a greatly disputed question as to how far and when a custom or usage among stock-brokers or at stock exchanges, may enter into and govern stock-brokers' contracts. At an early day the rule was laid down by the English courts, that he who buys or sells stock through a stock-broker must be considered as dealing with him according to the usages of the market in which he deals, and the customs which prevail in relation to that species of business.⁷

¹ *Colt v. Owens*, 90 N. Y. 368 (1882), holding that prices within thirty days after the sale is a reasonable rule. See also *Gruman v. Smith*, 81 N. Y. 25 (1880). *Capron v. Thompson*, 86 N. Y. 418 (1881). Cf. *Andrews v. Clerke*, 3 Bosw. 585 (1858).

² *Stratford v. Jones*, 97 N. Y. 586 (1885).

³ *Delevan v. Simonson*, 3 J. & S. 243 (1873).

⁴ *Clark v. Meigs*, 22 How. Pr. 240 (1873); 13 Abb. Pr. 467.

⁵ *Gruman v. Smith*, 81 N. Y. 25 (1880). See also *Capron v. Thompson*, 86 N. Y. 418 (1881).

⁶ *Schepeler v. Eisner*, 3 Daly, 11 (1869).

⁷ In the case of *Biederman v. Stone*, L. R., 2 Com. Pl. 504 (1867), the court says, "It has been held in a great number of cases that persons buying or selling stock or shares through members of the Stock Exchange, are bound by the rules which govern the transactions of that

body." To the same effect see *Bayliffe v. Butterworth*, 5 Railw. Cas. 283, per Parke, B.; *Mitchell v. Newhall*, 15 Mees. & W. 308 (1846); *Maxted v. Paine* (2d action), L. R., 6 Ex. 132 (1871); *Grissell v. Bristowe*, L. R., 4 C. P. 36, 47 (1868); *Appleman v. Fisher*, 34 Md. 540 (1871); *Coles v. Bristowe*, L. R., 4 Ch. App. 3; *Stray v. Russell*, 1 El. & El. 888 (1859); *Nickalls v. Merry*, L. R., 7 H. L. 530 (1875). Cf. *Pollock v. Stables*, 12 Q. B. 765 (1848); *Taylor v. Stray*, 2 C. B. N. S. 197 (1857); *Morrice v. Hunter*, 14 L. T. 897; *Kingsbury v. Kirwin*, 43 Super. Ct. 451 (1878); 77 N. Y. 612. But the usage must not be illegal. *Robinson v. Mollett*, L. R., 7 H. L. 802, 818, 826 (1874); *Hodgkinson v. Kelly*, 37 L. J. (Ch.) 837 (1868); *Taylor v. The Great Indian Peninsula Ry. Co.*, 4 De G. & J. 559, 573 (1859). Nor be the custom established by that one transaction. *Westropp v. Solomon*, 8 C. B. 345 (1849). It must be reasonable. *Goldschmidt v. Jones*, 32 L. T. N. S. 220. The usage may show how the

The American rule is more guarded, and allows usages of brokers to interpret the language of the contract, and where it is obscure to ascertain its nature and extent, but not to vary its terms, introduce new conditions, or authorize acts contrary to its provisions.¹ The customer may, however, by express agreement, waive his common law rights and allow usage to govern the transaction.²

business is to be transacted, but must not be unreasonable. *Rosenstock v. Tormey*, 32 Md. 169 (1869), holding also that the broker's correspondence with his city broker is not competent to prove purchases and sales. A usage that is contrary to an Act of Parliament, requiring the broker to notify his customer of the particular numbers of the shares purchased on his account, is void. *Perry v. Barnett*, L. R., 15 Q. B. D. 388 (1885). *Cf. Seymour v. Bridge*, L. R., 14 Q. B. D. 460 (1885).

¹ *Parsons v. Martin*, 77 Mass. 111 (1858); *Happer v. Sage*, 12 N. Y. Week. Dig. 78 (1881); *Lombardo v. Case*, 30 How. Pr. 117 (1865); 1 Add. Contr. (4th Am. fr. 8th Eng. ed. 1883), marg. p. 60, c. 2; 21 Am. L. Reg. N.S. 176. *Cf. Winans v. Hassey*, 48 Cal. 634 (1874). The case of *Baker v. Drake*, 66 N. Y. 518 (1876), holds that stock-brokers' usage cannot add to or make part of the contract. *Cf. Horton v. Morgan*, 19 N. Y. 170 (1859); *Peckham v. Ketchum*, 5 Bosw. 506 (1859); *Whitehouse v. Moore*, 13 Abb. 142 (1861). If there is doubt as to the existence of the usage the question is for the jury. *Dent v. Nickalls*, 29 L. T. 636 (1873). Upon the effect of usage in other transactions, see *Corn Ex. Bk. v. Nassau Bk.*, 91 N. Y. 74 (1883); *Richmond v. Union Steamboat Co.*, 87 N. Y. 240 (1881); *Walls v. Bailey*, 49 N. Y. 464 (1872); *Vail v. Rice*, 5 N. Y. 155 (1851); *Delafield v. State of Ill.*, 26 Wend. 192 (1841); *Dawson v. Kittle*, 4 Hill, 107 (1843); *Boardman v. Gaillard*, 1 Hun, 217 (1874); *Minn. C. Ry. Co. v. Morgan*, 52 Barb. 217 (1868); *Sipperly v. Stewart*, 50 Barb. 62, 68 (1867); *Duguid v. Edwards*, 50 Barb. 288 (1867); *Haskins v. Warren*, 115 Mass. 514, 536 (1874); *Dickinson v. Gay*, 89 Mass. 29; *Parrott v. Thatcher*, 26 Mass. 426 (1830);

Greenleaf v. Moody, 13 Allen, 363 (1866); *Tilley v. County of Cook*, 103 U. S. 155 (1880); *Natl. Bk. v. Burkhardt*, 100 U. S. 686 (1879); *Vermilye v. Adams Ex. Co.*, 21 Wall. 138 (1874); *Forrester v. Boardman*, 1 Story, 43 (1839); *Oelrichs v. Ford*, 23 How. 49 (1859); *Renner v. Bk. of Columbia*, 9 Wheat. 582 (1824); *Cape v. Dodd*, 13 Pa. St. 33 (1850); *Corbett v. Underwood*, 83 Ill. 324 (1876); *Phillip v. Moir*, 59 Ill. 155; *Bissell v. Ryan*, 23 Ill. 566 (1860); *Williams v. Gilman*, 3 Maine, 276 (1825); *Partridge v. Forsythe*, 29 Ala. 200 (1856); *Halwerson v. Cole*, 1 Spear (S. C.), 321 (1843); *Hagg v. Snaith*, 1 Taunton, 347 (1808); *Gibson v. Crick*, 1 H. & C. 142 (1862); *Fleet v. Murton*, L. R., 7 Q. B. 126 (1871).

² *Van Brunt, J.*, in *Robinson v. Norris*, 51 How. Pr. 442 (1874), says, in his clear and decisive diction, "It has been settled by our Court of Appeals that no custom among brokers can deprive parties of rights which the law gives them, but they have not decided that these rights may not be waived by agreement. I think 'it perfectly clear that if the broker informs his customer of the terms upon which he will act for him as his broker, and in view of that notice the customer gives an order, he is bound by the terms on which the broker proposed to act for him.'" See also *Baker v. Drake*, 66 N. Y. 578 (1876). See, in general, *Colket v. Ellis*, 32 Leg. Int. 82; *Sutton v. Tatham*, 10 Ad. & El. 25; *Bayley v. Wilkins*, 18 L. J. (C. P.) 273; *Duncan v. Hill*, L. R., 6 Ex. 255; *Sheppard v. Murphy, Jr.*, L. R., 2 Eq. 569; *Bowring v. Shepherd*, L. R., 6 Q. B. 309; *Evans v. Waln*, 71 Penn. St. 69; *Sweeting v. Pearce*, 7 C. B. N. S. 449; *Shaw v. Spencer*, 100 Mass. 382; *Day v. Holmes*, 103 Mass. 306.

CHAPTER XXVI.

PLEDGES AND MORTGAGES OF STOCK.

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| <p>§ 463. Definitions of pledge, mortgage, and lien.</p> <p>464. Mortgages and pledges of stock.</p> <p>465. How a pledge of stock arises or is made.</p> <p>466. Pledgee may have the stock registered in his own name or the name of another.</p> <p>467. Stock-broker purchasing stock for a customer on a margin is a pledgee.</p> <p>468. Miscellaneous rights of pledgee.</p> <p>469. Pledgee need not retain or return to the pledgor the identical certificates or shares of stock which were pledged, but must have equal quantity always on hand.</p> <p>470. Pledgee's liability on subscription and statutory liability on stock.</p> | <p>§ 471. Pledgee has no right to sell or repledge the stock, even temporarily.</p> <p>472. Purchasers or pledgees of stock from pledgee with notice are not protected.</p> <p>473. <i>Bona fide</i> repledgees or purchasers of pledged stock are protected.</p> <p>474. Pledges by agents, trustees, executors, &c., legally and in breach of trust.</p> <p>475. Pledgor's remedies.</p> <p>476. Pledgee's remedies when debt secured is not paid.</p> <p>477. Notice of sale of stock by pledgee to apply to debt secured.</p> <p>478. Formalities of sale.</p> <p>479. Pledgee himself cannot purchase at the sale.</p> |
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§ 463. *Definitions of pledge, mortgage, and lien.*—A pledge may be defined to be a delivery of personal property as a security for some debt or engagement. A mortgage of personalty, on the other hand, is a sale with the condition attached, that if the mortgagor performs some act, the sale shall be void. In a pledge, the title remains in the pledgor, while the pledgee has a special property in the thing pledged.¹ In a mortgage, the title passes to the mortgagee, subject to being revested in the mortgagor upon payment of the debt. In pledges, the thing pledged must be delivered to the pledgee. In mortgages, generally the possession of the thing mortgaged remains with the mortgagor. A pledge differs from a lien, in that a pledge, by implication, gives the pledgee a power to sell, on due notice, in case the debt is not paid on maturity, while a lien gives merely the power of detention until the debt is paid.²

¹ See 2 Parsons on Contracts, 113.

² Donald v. Suckling, L. R., 1 Q. B. 604, the court saying: "In the case of a simple lien there can be no power of sale or disposition of the goods which is in-

consistent with the retention of the possession by the person entitled to the lien; whereas, in the case of a pledge or pawn of goods, to secure the payment of money on a certain day, on default by the pawnor,

§ 464. *Mortgages and pledges of stock.*—Shares of stock may be the subject of a mortgage or pledge.¹ A mortgage of stock, however, is not often made, and unless there is a clear intent to the contrary, the courts will treat the transaction as a pledge, rather than a mortgage.² In fact it is difficult to ascertain from the cases, how shares of stock may be mortgaged, and a few early decisions, which held certain transactions to be mortgages, would, to-day, be held to be pledges.³ There are but few clear cases of

the pawnee may sell the goods deposited, and realize and become a trustee for the overplus for the pawnor, or even if no day of payment be named, he may, upon waiting a reasonable time, and taking the proper steps, realize his debt in like manner."

¹ "Nothing is better settled than that shares in the capital stock of a corporation are the subject of pledge." *Dayton National Bank v. Merchants Natl. Bk.*, 37 O. St. 208 (1891). "It was formerly doubted whether it [stock] could be the subject of a pledge, but it is now held that it can be." *Newton v. Fay*, 92 Mass. 505 (1865). The pledge may be for a running liability, and is not released by an extension of any particular debt. *Merchants Natl. Bk. v. Hall*, 83 N. Y. 338 (1881). Stock may be given by the debtor to his creditor, to sell for the benefit of the creditor, and the surplus to be returned to the debtor. *Beckwith v. Burroughs*, 13 R. I. 294 (1881). This probably makes the creditor the agent of the debtor. The pledge may be to secure the carrying out of a contract. *Vaupell v. Woodward*, 2 Sandf. Ch. 143 (1844). If the loan secured by the pledge of stock is, usurious, the pledgor may recover back the stock without payment. The pledge is void. *Cousland v. Davis*, 5 Bosw. 619 (1859). The pledge of stock may provide that for part payments of the debt, the pledgor may withdraw part of the stock pledged. *First Natl. Bk. v. Root*, 8 Northeast Rep. 105 (Ind., 1886).

² *Newton v. Fay*, *supra*; *Nabring v. Bank of Mobile*, 58 Ala. 204 (1877); *Merchants Bk. v. Cook*, 4 Pick. 405 (1826); *Mechanics, &c., Association v. Conover*, 14 N. J. Eq., 219 (1862).

³ Thus in *Huntington v. Mather*, 2 Barb. 538 (1848), the court truly says: "There are two leading considerations to be regarded in determining whether the transaction is a pledge or a mortgage, namely; the title and the possession. If

it is a mortgage, the legal title passes to and is vested in the creditor. With a pledge it is different, the legal title, until a sale on default of payment or redemption, continuing in the pledgor.

The essential difference as to matter of right, is that in one the title passes, and in the other it does not. But the difference in substance and fact, is that in the case of a pawn or pledge, the possession must pass out of the pawnor, but in the case of a mortgagor it need not." The court, however, influenced probably by the equities of the case, held the transaction to be a mortgage, and that the right of the debtor to redeem was barred by the ten year Statute of Limitations. In the case of *Smith v. 49* and *56 Quartz Min. Co.*, 14 Cal. 242 (1859), the court held the transaction to be a mortgage rather than a conditional sale of the stock. The question of pledge was not considered. *Manns v. Brookville Natl. Bank*, 73 Ind. 243 (1881); speaks of the transaction as a mortgage, and *Williamson v. New Jersey Southern R. R. Co.*, 26 N. J. Eq. 398 (1875), says that such a mortgage need not be recorded in the municipal clerk's office, as required by the chattel mortgage act. In both cases, the transaction might better have been treated as a pledge. In *Adderly v. Storm*, 6 Hill, 624 (1844), the court said: "I have already said that this was not a pawn or pledge of the stock, neither was it strictly a mortgage." At the present day it would be held to be a pledge. *Wilson v. Little*, 2 N. Y. 443 (1849); *Hasbrouck v. Vandervoort*, 4 Sand. 74 (1850). In the case *Brewster v. Hartley*, 37 Cal. 15 (1869), the court says: "The transfer in writing of shares of stock, not only does not prove that the transaction is not a pledge, but the stock, unless it is expressly made assignable by the delivery of the certificates, cannot be pledged in any other manner."

a mortgage of stock to be found. It seems that a formal instrument of chattel mortgage of stock, duly executed and registered at the municipal clerk's office, as required by law in case of chattel mortgages, would not constitute an effectual mortgage of stock, and the mortgagee would not be protected, where he does not receive the certificate of stock from the mortgagor, or does not obtain a registry of transfer on the corporate books.¹ Where, on the other hand, the certificate of stock is delivered to the creditor as security, it is evident that possession of the property is given to the creditor, but that the debtor still considers the stock to be his. Such a transaction is a pledge, and not a mortgage, and consequently, since the giving of stock certificates as security is almost invariably effected by a delivery of the certificates, a mortgage of stock may be said to be possible but not probable or even sensible. The delivery of a certificate of stock with a blank power of attorney, as collateral security, constitutes a pledge and not a mortgage,² and the same rule provides even though an absolute transfer or registry is made on the corporate books.³

§ 465. *How a pledge of stock arises or is made.*—A pledge of stock is generally made by a delivery of the certificates of stock, indorsed in blank, to the pledgee, and a memorandum in writing to the effect that the stock is held in pledge is generally signed and given to the pledgor, and a copy thereof attached to the certificates of stock.⁴ A mere delivery of the certificate of stock indorsed in blank, however, is sufficient to constitute a

¹ The clearest and most satisfactory case is *Spalding v. Paine's Admr.*, 81 Ky. 416 (1883), where a chattel mortgage of a share of stock was duly recorded in the proper county, the mortgagor retaining the certificate of stock. The mortgagor subsequently sold and transferred the certificate of stock to a *bona fide* purchaser. The court held that the recording of the mortgage was of no avail, that there could be no mortgage of choses in action, and that the *bona fide* transferee took the stock. Pryor, J., well says: "Much of the business of the country is conducted on the faith of the pledge of such stock as collaterals, and to adjudge that the holder of the stock by transfer on the books of the corporation, or by indorsement and delivery by the owner, is subordinate in his claim to the mortgagee, upon the doctrine of constructive

notice, would paralyze trade and open a wide field for the fraudulent disposition of such valuable interests at the expense of honest and confiding purchasers." *Of. Manns v. Brookville Natl. Bk.*, 73 Ind. 243 (1881); *Foster v. Potter*, 37 Mo. 525; *Vowell v. Thompson*, 3 Cranch, 428 (1829).

² *Mechanics B. & L. Association v. Conover*, 14 N. J. Eq. 219 (1862); *Lewis v. Graham*, 4 Abb. Pr. 106 (1857).

³ *Nabring v. Bank of Mobile*, 58 Ala. 204 (1877); *Wilson v. Little*, 2 N. Y. 443 (1849).

⁴ In a few cases, a mere delivery of the certificate without a written transfer has been held sufficient to constitute a pledge. See *Brewster v. Hartley*, 37 Cal. 15; *Jarvis v. Rogers*, 13 Mass. 105; *Robinson v. Hurley*, 11 Iowa, 410, but see *Lollande v. Ingram*, 19 La. Ann. 364 (1867); *United States v. Cutts, Sumner*, 133.

pledge, without any memorandum in writing to that effect, and without a registry of the same being made on the corporate books.¹ Not even a provision of the charter or a by-law of the corporation to the effect that transfers are not valid until registered on the corporate books, can prevent a pledge of stock being made by a mere delivery of the certificates indorsed in blank, or indorsed to the pledgee, without such registry.² The provision requiring such registry would seem not to concern the pledgee in any way, except that he could not claim the dividends without the registry, and in a few States where an attachment of the stock for the pledgor's debts would cut off a previous unregistered vendee's or pledgee's rights, he, by not registering, encounters that risk.³ A transfer of stock, whether registered on the corporate books or not, may be shown to be a pledge, and parol evidence is admis-

¹ *Mount Holly, &c., Co. v. Ferree*, 17 N. J. Eq. 117 (1864); *Finney's Appeal*, 59 Penn. St. 398 (1868); *Blouin v. Liquidators, &c.*, 30 La. Ann. 714 (1878); *Merchants Natl. Bk. v. Richards*, 6 Mo. App. 454 (1879); *aff'd* 74 Mo. 77; *Broadway Bk. v. McElrath*, 13 N. J. Eq. 24 (1860); *Cornick v. Richards*, 3 Lea, 1 (1879); *Baldwin v. Canfield*, 26 Minn. 43 (1879); *Pitot v. Johnson*, 33 La. Ann. 1286 (1881); *New Orleans Natl. Banking Assn. v. Wiltz*, 10 Fed. Rep. 330 (1881); *Continental Natl. Bk. v. Eliot Natl. Bk.*, 12 Rep. 35 (1881). *Cf.* *State v. First Natl. Bk.*, 89 Ind. 302 (1883). The pledgor may by word of mouth, extend stock already pledged to further advancements by the pledgee. *Van Blarcom v. B'way Bk.*, 9 Bosw. 532 (1862).

² *McNeil v. Tenth Natl. Bank*, 46 N. Y. 325 (1871); *Dickinson v. Central Natl. Bk.*, 129 Mass. 279 (1880); *Fraser v. Charleston*, 11 S. C. 486 (1878); *Factors & T. Ins. Co. v. Marine D. D. Co.*, 31 La. Ann. 149 (1879); *Pitot v. Johnson*, 33 La. Ann. 1286 (1881); *Continental Natl. Bk. v. Eliot Natl. Bk.*, *supra*; *Lowry v. Com. Bank, Taney*, 310 (1848); *Blouin v. Liquidators, &c.*, 30 La. Ann. 714 (1878); *Lightner's Appeal*, 82 Penn. St. 301; *United States v. Cutts*, 1 Sumn. 133 (1832); *Leitch v. Wells*, 48 N. Y. 585 (1872); *Commercial Bk. of Buffalo v. Kortright*, 22 Wend. 348 (1839); *aff'd* 20 Wend. 91; *Otis v. Gardner*, 105 Ill. 436 (1883). As regards such provisions requiring registry, a pledge of stock stands on the same footing as a sale of stock. The unregis-

tered pledge is protected against the pledgor's assignee in bankruptcy. *Re Shelly*, 34 L. J. (Bankr.) 6 (1865).

³ Thus in States where an attachment has precedence over not only transferees without registry made after the attachment is levied, but over unregistered transfers made before the levy of attachment, a pledge, like a sale of stock, is protected against attachment on the pledgor's debts, only by registry. *Weston v. Bear R. & A. Co.*, 5 Cal. 186 (1855); *Williams v. Mechanics Bank*, 5 Blatch. 59 (1862); *State Ins. Co. v. Sax*, 2 Tenn. Ch. 507 (1875); *State v. First Natl. Bk.*, 89 Ind. 302 (1883); *Shipman v. Aetna Ins. Co.*, 29 Conn. 245 (1860); *Pinkerton v. Manchester, &c., R. R. Co.*, 42 N. H. 424 (1861); *Oxford Turnpike Co. v. Brund*, 6 Conn. 552 (1827). *Cf.* *Strout v. Natoma W. & M. Co.*, 9 Cal. 78 (1858). But the purchaser at the execution sale is not protected against the pledgee, if he purchased with notice. *Weston v. Bear, R. & A. Co.*, 6 Cal. 425 (1856). And if notice of the pledge is given to the corporation, the pledgee is protected against attachments, although no registry is had. *State Ins. Co. v. Gennett*, 2 Tenn. Ch. 100 (1874). As regards the ordinary rights of stockholdership, it is no object to the pledgee to obtain registry. Even if registered he cannot vote nor have a voice in corporate meetings. See § 468. As to the dividends, however, he is entitled to them, as against the pledgor, but, of course, can obtain them from the corporation only by obtaining registry.

sible to prove that fact.¹ A mere direction to the corporation cannot constitute a pledge.² But where no certificate has been issued to the stockholder, he may pledge the stock by an instrument in writing.³ A corporation may pledge its unissued stock,⁴ but there is a difference of opinion as to whether the pledgee is liable as an absolute stockholder on such stock.⁵

§ 466. *Pledgee may have the stock registered in his own name or the name of another.*—Where certificates of stock, indorsed in blank, are delivered to a person, in pledge, as collateral security for a debt or for any other purpose, the pledgee may fill in the blanks and have the stock registered in his own name, on the corporate books,⁶ or the pledgee may have the stock registered in the name of another person, in order that he may protect his special property in the stock and at the same time not be liable thereon.⁷

§ 467. *Stock-broker purchasing stock for a customer on a margin is a pledgee of the stock.*—It has been well established that where a stockholder purchases stock on an order from his

¹ *Brick v. Brick*, 98 U. S. 514 (1878); *Wilson v. Little*, 2 N. Y. 443 (1849); *Ginz v. Stumph*, 73 Ind. 209 (1880); *Newton v. Fay*, 92 Mass. 505 (1865); *McMahon v. Macy*, 51 N. Y. 155 (1872); *Becher v. Wells Flouring Mill Co.*, 1 Fed. Rep. 276 (1880); *Burgess v. Seligman*, 107 U. S. 20 (1882); *Pinkerton v. R. R. Co.*, 42 N. H. 424.

² *Cumming v. Prescott*, 2 Y. & C. (Ex.) 488 (1837); *Lallande v. Ingram*, 19 La. Ann. 364 (1867), the court saying: "In all cases of pledge, the pledgee must be put in possession of the thing pledged, and if it be a claim, the evidence of the obligation must be transferred and delivered. Shares in stock cannot be pledged unless they be evidenced by certificates which must be transferred and delivered to the pledgee." But see note 4, § 465, *supra*.

³ *First Natl. Bk. v. Gifford*, 47 Iowa, 575 (1877), where such a pledgee was protected against a third person who had advanced the money to the pledgor to purchase the stock.

⁴ *Brewster v. Hartley*, 37 Cal. 15 (1869); *Fisher v. Seligman*, 7 Mo. App. 383; *Griswold v. Seligman*, 72 Mo. 110 (1880); *Burgess v. Seligman*, 107 U. S. 20 (1882); *Melvin v. Lamar Ins. Co.*, 80 Ill.

446 (1875); *Protection Ins. Co. v. Osgood*, 93 Ill. 69.

⁵ See Ch. XIV, § 247.

⁶ *Hubbell v. Drexel*, 21 Am. L. Reg. N. S. 452 (1881); *Re Angelo*, 5 De G. & S. 278 (1852); *Horton v. Morgan*, 19 N. Y. 170 (1869); *Union & P. Bk. v. Farrington*, 13 Lea (Tenn.), 333 (1884); *Hiatt v. Griswold*, 5 Fed. Rep. 573 (1881), holding also that a surety is not thereby discharged. *Day v. Holmes*, 103 Mass. 306 (1869), the court saying: "The delivery to them of the assignment in blank necessarily implied the right to insert their own names, and the doing so and taking out of new certificates was in accordance with the implied contract of the parties, and a lawful and reasonable measure to protect their security, and can upon no principle be deemed an unlawful conversion." *Fitchburg Sav. Bk. v. Torrey*, 134 Mass. 239 (1883), also holding that a release of the stock by the pledgee releases a surety. *Fay v. Gray*, 124 Mass. 500 (1878). Corporation must allow the registry. *Cornick v. Richards*, 3 Lea (Tenn.), 1 (1879).

⁷ *Day v. Holmes*, *supra*; *Heath v. Griswold*, 5 Fed. Rep. 573; *Anderson v. Philadelphia Warehouse Co.*, 111 U. S. 479 (1884). See also § 470.

customer, and the customer does not pay for the stock, but deposits with the broker a sum of money called a "margin," to protect the broker against loss, the broker is bound to have on hand the stock so purchased during the entire time of the contract, and has the rights, duties, and liabilities of a pledgee, with the customer as a pledgor.¹ The broker under such circumstances must conform to all the rules governing a pledgee's attitude towards a pledgor. He cannot repledge, nor sell without due notice, unless such rights be waived by the customer, the pledgor.²

§ 468. *Miscellaneous rights of pledgee.*—Dividends declared during the continuance of the pledge belong to the pledgee, even though the latter is not registered as owner on the corporate books.³ It has been held that a pledgee may bring an action to protect the corporate interests where a full stockholder would not be allowed to sue, for the reason that the latter has the power to affect the management by his vote. A pledgee has not the right to vote on the pledged stock even though he is registered as a stockholder.⁴ If so registered the pledgor may compel him, by legal proceedings, to give a proxy for voting purposes.⁵ A pledgee is not bound to protect the stock from forfeiture, for non-payment of calls.⁶ The pledgee is entitled to the dividends on the stock, but must account for them when the pledge is redeemed.⁷ A pledgee of certificates of stock is protected against further sales or pledges of the same stock by the pledgor, such other sales or pledges being without the delivery of any certificate, the same as the vendee of a certificate of stock is protected against another sale of the stock to a purchaser who takes without any certificate.⁸ The possession of the certificate protects the pledgee herein.

¹ Baker v. Drake, 66 N. Y. 518 (1876); Markham v. Jaudon, 41 N. Y. 235 (1869), and see Chapter XXV.

² See Chapter XXV.

³ Herrman v. Maxwell, 47 Super. Ct. 347 (1881), and the pledgor who collects them holds them in trust for the pledgee. Hill v. Newichawanick Co., 48 How. Pr. 427 (1874).

⁴ Baldwin v. Canfield, 26 Minn. 43 (1879). See also Merchants' Bk. v. Cook, 4 Pick. 406; *Ex parte* Willcock, 7 Cowen, 402; McDaniels v. Flower, &c. Co., 22 Vt.

274; Laws of N. Y. 1850, ch. 140, § 5; Butterworth v. Kennedy, 6 Bosw. 143.

⁵ See Ch. XXXVII.

⁶ Southwestern R. R. Bk. v. Douglas, 2 Spear (S. C.), 329 (1844).

⁷ Isaac v. Clarke, 2 Bulst. 306; Hasbrouck v. Vandervoort, 4 Sandf. 74; Edwards on Bailments, 300.

⁸ Maybin v. Kirby, 4 Rich. Eq. 106. See § 321. The cases therein cited are partly cases of pledge and partly of sale of certificates of stock. The rule applies equally to both.

§ 469. *Pledgee need not retain or return to the pledgor the identical certificates or shares of stock which were pledged, but must have equal quantity always on hand.*—One share of stock does not differ from another share in the same capital stock. Each is but an undivided interest in the corporate rights, privileges, and property. Accordingly, it is held that a pledgee of stock need not retain in his possession the identical shares of stock which were pledged to him, but that the rights of the pledgor are fully preserved if similar stock is returned to him upon the termination of the pledge.¹ But the pledgee must have on hand at all times a sufficient quantity of the stock pledged, whether the debt secured is due or not, since the law will not allow the pledgee to speculate or deal with the stock of another as though it was his own.² It is insufficient that he can at once procure the stock from one to whom it is loaned,³ or that he had sufficient on hand for the plaintiff pledgor, but not enough for all the pledgors whom he had at any particular time.⁴ The law requires him to set aside so much stock as has been pledged to him.

§ 470. *Pledgee's liability on subscription and statutory liability on stock.*⁵—A pledgee who has obtained registry on the corporate books appears to third parties as a full stockholder. Accordingly, in case the corporation becomes insolvent, the registered pledgee is held liable on his stock, as though he were an absolute stockholder. In order to avoid this danger, the law allows the pledgee to have the pledged stock registered on the corporate books in the name of a nominee of the pledgee.⁶

¹ *Nourse v. Prince*, 4 Johns. Ch. 490 (1820); *Id.* 7 Johns. Ch. 69 (1823); *Horton v. Morgan*, 19 N. Y. 170 (1859); *Barclay v. Culver*, 30 Hun, 1 (1883); *Noyes v. Spaulding*, 27 Vt. 420 (1855); *Atkins v. Gamble*, 42 Cal. 86; *Price v. Grover*, 40 Md. 102 (1874); *Gilpin v. Howell*, 5 Penn. St. 41 (1846); *Hardenburgh v. Bacon*, 33 Cal. 356 (1867); *Taylor v. Ketchum*, 35 How. Pr. 289 (1867); *Langton v. Waite*, L. R. 6 Eq. 165 (1868); *Thompson v. Toland*, 48 Cal. 99 (1874); *LeCray v. Eastman*, 10 Mod. 499 (1735); *Hubbell v. Drexel*, 21 Am. L. Reg. N. S. 452 (1881); *Boylan v. Huguet*, 8 Nev. 345 (1873). In the case *Dykers v. Allen*, 7 Hill, 497 (1844), the pledgee at one time seems to have had no stock on hand. In

selling the pledgor's stock, on notice, for non-payment of the debt, the pledgee need not sell the identical stock pledged. *Berlin v. Eddy*, 33 Mo. 426 (1863).

² *Ex parte Dennison*, 3 Ves. 552 (1797); *Taussig v. Hart*, 58 N. Y. 425 (1874); *Thompson v. Toland*, 48 Cal. 99 (1874); *Hubbell v. Drexel*, 21 Am. L. Reg. N. S. 452 (1881). The pledgor may waive this restriction by express agreement. *Ogden v. Lathrop*, 65 N. Y. 158 (1875).

³ *Dykers v. Allen*, 3 Hill, 593; 7 Id. 497 (1844); *Ex parte Dennison*, *supra*.

⁴ *Fay v. Gray*, 124 Mass. 500 (1878).

⁵ See Ch. XIV, § 247.

⁶ *Newry, &c. Ry. Co. v. Moss*, 14 Beav. 64 (1851). See § 466.

Where such a registry is obtained the pledgee has the advantage of a control of the stock, and at the same time escapes the dangers of liability as an ordinary stockholder.

§ 471. *Pledgee has no right to sell or repledge the stock, even temporarily.*—This necessarily follows from the principle of law that a pledgee of stock must retain constantly in his possession, shares of stock equal in quantity to that pledged; that the pledgee cannot legally part with the possession of such stock by a sale or repledge of it; and that if he does so he is guilty of a conversion.¹ In Pennsylvania it is a penal offense for the pledgee

¹ *Goss v. Hampton*, 16 Nev. 185 (1881). The case of *Ex parte Sargent*, L. R. 17 Eq. 273 (1874), contained a *dictum* giving a contrary rule, but the case of *France v. Clark*, L. R. 22 Ch. Div. 830 (1883), disapproves such *dictum* and says: "As a general rule the pawnee of chattels has no right to sell them, unless a time was originally fixed for their redemption, and that time has expired, or unless he had made a demand upon the pawnor for the payment of what is due to him." In *Langton v. Waite*, L. R. 6 Eq. 165 (1868), the court says: "The law is clear that in the absence of express contract to the contrary, a pawnee cannot sell without the express permission of the owner, and that if he does, the owner can charge him with the excess of the price over the loan." The court, however, seemed to think that the pledgee could repledge the stock. *Fay v. Gray*, 124 Mass. 500 (1878), holds that the pledgee has no right to sell, lend, or repledge the stock. In the notes contained in 21 Am. Law Reg. N. S. 454, a contention is made that the pledgee should be allowed to repledge, but it is admitted that the weight of authority holds otherwise. The following cases are cited: *Bank v. Trenholm*, 12 Heisk. (Tenn.) 520; *Bank v. Bryce*, 19 Am. Law Reg. N. S. 503; *Tausig v. Hart*, 58 N. Y. 425 (1874); *Work v. Bennett*, 70 Penn. St. 484; *Wood v. Hayes*, 15 Gray, 375; *Thompson v. Patrick*, 4 Watts (Pa.), 414, and see § 469. In *Gould v. Farmers' Loan & Trust Co.*, 23 Hun, 322 (1880), the court said that the pledgee might repledge the stock to the extent that he had in it. In *Lawrence v. Maxwell*, 53 N. Y. 19 (1873), the court says: "Ordinarily and in the absence of any agreement or assent by the pledgor, the pledgee would have no right to use the thing pledged, and a use of it

would be illegal. But, under special circumstances, depending somewhat upon the nature of the pledge, and in all cases, with the assent of the pledgor, express, or implied, the property pledged may be used by the pledgee in any way consistent with the general ownership, and the ultimate rights of the pledgor." Story on Bailments, § 324, says: the pawnee "may sell or assign all his interest in the pawn, or he may convey the same interest conditionally, by way of pawn, to another person, without in either case destroying or invalidating his security." See also *Talty v. Freedman's Sav., &c. Co.* 93 U. S. 321 (1876); 2 Kent's Com. 579; *Jarvis v. Rogers*, 13 Mass. 105; 15 Id. 389, 408; *Mores v. Conham, Owen*, 123; *Ratcliffe v. Davis*, 1 Buls. 29; *Anon.* 2 Salk. 522. The right of the pledgee to repledge may exist by force of a custom understood by both parties. *Chamberlain v. Greenleaf*, 4 Abb. N. C. 178 (1878). In the case, *Lewis v. Mott*, 36 N. Y. 394 (1867), where after the debt was due and unpaid the pledgee turned over the debt and security to another, without a foreclosure or sale on notice, the court held that the latter could hold the collateral stock until the pledgor tendered the amount of the debt. The latest English cases hold that although the repledge may be wrong, yet that the pledgor cannot reclaim the stock from the repledgee until the former pays the debt for which the pledge was made. *Donald v. Suckling*, L. R. 1 Q. B. 585; *Halliday v. Holgate*, L. R. 3 Ex. 299. Where a broker holding stock in pledge on a margin, repledges it without the consent of his customer, it has been held that he cannot recover the value of the stock from the customer on a tender of the certificate. *Clarkson v. Snider*, 5 Canadian Law Times, 587 (1885).

to repledge the stock.¹ Although apparently, the pledgor would not be injured by the pledgee's transferring to another the debt and the stock pledged as collateral security, yet the law rigidly protects the interests of the debtor and pledgor and will not compel him to submit to the danger and trouble of transfers by the pledgee to distant or irresponsible persons. There may, of course, be an express agreement or understanding to the contrary.

§ 472. *Purchasers or pledgees of stock from pledgee with notice are not protected.*—A person who purchases or takes in pledge stock which he knows is held in pledge by the person from whom he takes it, is not a *bona fide* holder of such stock, and is not entitled to the rights of such. At the best he stands merely in the place of the pledgee from whom he receives the stock. He must restore the stock to the owner, in case the pledgee would be obliged to restore it, had no second sale or pledge been made. The second pledgee or vendee, with notice that he was taking pledged stock, has no rights which the first pledgee has not. He is but an equitable assignee of the latter, and can be compelled by the owner to deliver the stock, in any case where the first pledgee could be so compelled.² The same rule applies whether the pledgee assigns or repledges both the debt and the stock, or the stock alone.³

§ 473. *Bona fide repledgees or purchasers of pledged stock are protected.*—Where, however, a pledgee of certificates of stock indorsed in blank takes the certificates and sells or pledges them to another, who takes such certificates in good faith and for value and without notice that his vendor or pledgor held them as a pledge, the purchaser or pledgee from the pledgee is as fully protected in his rights as though the person with whom he dealt

¹ Act of May 25th, 1878 (Purdon's Digest, 2107), modified as to purchases by broker on margin, by Act of June 10th, 1881 (P. L. 1881, 107).

² Any fact, such as usury in the second transaction, which prevents the second pledgee or purchaser from being a *bona fide* purchaser, applies to a repledgee of stock. The repledgee is not protected. *Felt v. Heye*, 33 How. Pr. 359 (1862); *Little v. Barker*, 1 Hoff. Ch. 487 (1840). So also where the repledgee takes in consideration of a pre-existing indebtedness. *Ashton's Appeal*, 78 Penn.

St. 153 (1873). A bank receiving a collection with collateral is not entitled to the latter, where it becomes insolvent before the collection is remitted. *Corn Exchange Bank v. Blye*, N. Y. Daily Reg. Sept. 9th, 1886. In general, see also *Duncan v. Jaudon*, 15 Wall. 165; *Shaw v. Spencer*, 100 Mass. 382; *Ellis Appeal*, 8 Weekly Notes of Cases (Penn.), 538; *Porter v. Parks*, 49 N. Y. 564.

³ *Felt v. Heye*, *supra*. Nor can the repledgee claim the benefit of the debt not assigned to him. See also *Talty v. Freedman's, &c. Co.*, 93 U. S. 321 (1876).

was the absolute owner of the stock.¹ This rule arises not on the ground that the certificate of stock is negotiable, but for the reason that the owner is held to have enabled his pledgee to sell the stock as the pledgee's own, and that as between the owner and the *bona fide* purchaser or pledgee from the pledgee the owner must bear the loss. The law of estoppel prevents his denying the right of his pledgee to sell or pledge, as against a *bona fide* purchaser or pledgee from the pledgee. So, also, under the well established rule that where one of two innocent parties must suffer from the fraud of a third, the loss must fall upon him who enabled the third party to perpetrate the fraud. If the pledgee has repledged the stock the owner can obtain his stock only by paying to the repledgee the amount of the latter's advancement to the first pledgee.² The pledgor of stock under these rules has practically no protection as to his stock, except the honesty and responsibility of his pledgee. The *bona fide* purchaser or pledgee from the pledgee is equally protected whether the certificates of stock are indorsed by the pledgor or vendor, or are indorsed in blank by some previous holder.³ The repledgee or vendee is held to be a *bona fide* holder, only where, in general, he would be held so to be.⁴

¹ The important case of *McNeil v. Tenth Nat'l Bank*, 46 N. Y. 325 (1871), was on the rights of a *bona fide* repledgee of stock and fully sustains the general rule. See also *Fatman v. Lobach*, 1 Duer, 354 (1852); *Wood's Appeal*, 92 Penn. St. 379 (1880); *Wood v. Smith*, 8 Week. Notes, 441; *Goss v. Hampton*, 16 Nev. 185 (1881); *Mount Holly, &c., Co. v. Ferree*, 17 N. J. Eq. 117 (1864); *Otis v. Gardner*, 105 Ill. 436 (1883); *Ex parte Sargent*, L. R. 17 Eq. 273 (1874); *Cherry v. Frost*, 7 Lea (Tenn.), 1 (1881), the court saying that in general a pledgee of personal property cannot convey a good title to another, but "if the owner intrusts to another not merely the possession of the property but also written evidence over his own signature of title thereto, and of unconditional power of disposition over it, the case is vastly different." In the case *Ortigosa v. Brown*, 47 L. J. (Ch.) 168 (1878), the court, following the English doctrine that an unregistered transferee of certificates of railway stock has no more rights than his transferrer, refused to protect the unregistered repledgee of stock.

² *Wood's Appeal*, 92 Penn. St. 379

(1880); *Fatman v. Lobach*, 1 Duer, 354 (1852); *Ex parte Sargent*, L. R. 17 Eq. 273 (1874); *Cherry v. Frost*, 7 Lea (Tenn.), 1 (1881), holding, however, that payments on the subscription by the owner, subsequently to the repledge, does not inure to the benefit of the latter. If the repledgee has other collateral also, it will be applied to the debt before the repledged stock is applied. *Gould v. Farmers Loan & Trust Co.*, 23 Hun, 322 (1880). See in general, *Donald v. Suckling*, L. R. 1 Q. B. 585; *Moore v. Conham*, Owen, 123; *Ratcliffe v. Davis*, Yelv. 178; *Johnson v. Cumming*, Scott's C. B. N. S. 331; *Jarvis, Adm'r v. Rodgers*, 15 Mass. 369.

³ *Goss v. Hampton*, 16 Nev. 185 (1881).

⁴ In California the peculiar doctrine is sustained that the word "trustee" on the face of the certificate is no notice, and does not deprive the pledgee of his character of being a *bona fide* holder. *Brewster v. Sime*, 42 Cal. 139 (1871); *Thompson v. Toland*, 48 Cal. 99 (1874). If the repledgee receives the stock as security for an antecedent indebtedness he is not a *bona fide* holder. *Gould v. Farmers Loan & Trust Co.*, 23 Hun, 322

§ 474. *Pledges by agents, trustees, executors, &c., legally and in breach of trust.*—It is within the power of an executor or administrator to pledge shares of stock belonging to the estate, and the pledgee is protected, even though he knew that the executor pledged it as an executor.¹ A trustee, on the other hand, has no implied power to pledge or sell corporate stock belonging to the trust.² An agent's pledges of his principal's stock follow the same rules as where a pledgee repledges the stock given to him in pledge. A *bona fide* holder for value and without notice is protected, while one who takes with notice is not protected. Where, however, the one taking stock in pledge from an agent knows that the latter is acting as agent, he is bound to inquire whether the principal has authorized his agent to pledge the stock, since a power to pledge cannot be presumed from a power to sell.³ The right of corporations and persons to give and take stock in pledge is also treated of elsewhere.⁴

§ 475. *Pledgor's remedies.*—Where the pledgee of stock has been guilty of a conversion of it, the pledgor's remedy against him is generally by an action at law for damages. He need not tender to the pledgee the amount of the debt secured by the pledge, since the pledgee may recoup to that extent and thus decrease the damages of the pledgor.⁵ The pledgor's damages are measured by the market value of the stock at the time of the conversion; together with interest and subsequent damages.⁶ The pledgor may be barred from his action for damages by a waiver of the particular act of conversion by the pledgee.⁷ He has the

(1880). A pledgee is not *bona fide* when the name of another pledgee in the certificate is erased and his own inserted. *Denny v. Lyon*, 38 Penn. St. 98 (1860).

¹ *Goodwin v. American Nat'l Bk.*, 48 Conn. 550 (1881); *Wood's Appeal*, 92 Penn. St. 379 (1880); *Carter v. Mfs. Nat'l Bk.*, 71 Me. 448 (1880), and see Ch. XIX, § 329.

² See Ch. XIX §§ 323–327; *Shaw v. Spencer*, 100 Mass. 382 (1868).

³ See Ch. XIX, § 321.

⁴ See Chapter XIX.

⁵ *Allen v. Dykers*, 3 Hill, 93 (1842); 7 Id. 497; *New York, L. E. & W. R. R. Co. v. Davies*, 38 Hun, 477 (1886); *Work v. Bennett*, 70 Penn. St. 484 (1872); *Fisher v. Brown*, 104 Mass. 259; *Neiler v. Kelly*, 69 Penn. St. 403 (1871); *Langton v. Waite*, L. R. 6 Eq. 165 (1868); *Felt v. Heye*, 23 How. Pr. 359 (1862); *Lewis*

v. Graham, 4 Abb. Pr. 106 (1857); *Cortelyou v. Lansing*, 2 Caines' Cas. 200. However a later case in Massachusetts, *Cummock v. Institution for Sav.*, 34 Alb. L. J. 208 (1886), holds that a tender of payment of a debt is necessary to enable a pledgor to maintain trover for a conversion of property pledged, unless the lien created by the pledge has been otherwise discharged.

⁶ See Ch. XXXV. In *Fowle v. Ward*, 113 Mass. 548 (1873), the court said the damages should be "a sum of money which would enable him to purchase seventeen new shares to replace those which have been taken from him, with such additional sum as would indemnify him for the dividends which he has lost since the sale, and also an equitable allowance for interest."

⁷ *Child v. Hugg*, 41 Cal. 519 (1871).

option, however, of ratifying a conversion by an unauthorized sale and claiming the proceeds, or he may repudiate the sale and sue for conversion.¹ The pledgor may, if he prefers, begin suit in a court of equity, when the pledgee has converted the stock, and compel him either to replace the stock or give compensation in damages. The jurisdiction of a court of equity in such a case has been questioned,² but has been sustained on the ground that only a court of equity can compel the pledgee to replace the stock or to take an accounting of the dividends declared while the pledge was running, or to reach third persons to whom the pledgee has assigned the debt and pledge.³ A pledgor cannot compel his pledgee to sell the stock and apply the proceeds to the debt by a notice to make such a sale.⁴ When the pledgee causes the stock to be sold the pledgor is entitled to the surplus proceeds of the sale remaining after the debt and the expenses of the sale have been paid.⁵

§ 476. *Pledgee's remedies when debt secured is not paid.*—

Where shares of stock are pledged as collateral security for a debt and the debt is not paid, and the pledgee wishes to apply the stock to the payment of the debt, he has the right to pursue either one of two remedies: he may file a bill in equity for the foreclosure and sale of the pledge,⁶ or he may give notice to the pledgor of

¹ *Atkins v. Gamble*, 42 Cal. 86, 91 (1871).

² *Genet v. Howland*, 45 Barb. 560 (1866).

³ *Bryson v. Raynor*, 25 Md. 424 (1866); *Conyngham's Appeal*, 57 Penn. St. 474 (1868); *Hasbrouck v. Vandervoort*, 4 Sand. 74 (1850). Where the replledgee converts the stock the remedy for conversion is with the first pledgee, not with the first pledgor. *Thompson v. Toland*, 48 Cal. 99 (1874). The pledgee must return the stock and stock dividends and account for money dividends. *Vaughan v. Wood*, 1 M. & K. 403 (1833). The assets applicable to the debt will be marshalled. *Hurbert v. Mechanics Bldg. & Loan Ass'n*, 17 N. J. Eq. 497 (1864), and the pledgor's interests protected. *Gould v. Farmers L. & T. Co.*, 23 Hun, 322 (1880). In case of a wrongful replledge the pledgor may claim the proceeds or redeem the stock from the second pledgee. *Chamberlain v. Greenleaf*, 4 Abb. N. C. 178 (1878). Where the second pledgee has sold the stock for non-payment of his debt,

the first pledgor may claim the excess, the amount retained by the replledgee being more than the first pledgor's debt. *Re Bonner*, 3 Daly, 75 (1878).

⁴ *Lawrence v. Maxwell*, 53 N. Y. 19; *Robinson v. Hurley*, 11 Iowa, 412; *O'Neill v. Whigham*, 88 Penn. St. 394; *Rozet v. McClellan*, 48 Ill. 345; *Smouse v. Bail*, 1 Grant, 397; *Taggard v. Centenius*, 15 Wend. 155; *Fisher v. Fisher*, 98 Mass. 303; *Napier v. Central, &c. Bk.*, 68 Ga. 637, holding, however, that where the pledgee does not sell, because he and others were "bearing" the market, there may be an element of fraud which gives a cause of action.

⁵ And the pledgor's assignee for the benefit of creditors may claim it. The pledgee bank has no banker's lien on the surplus for other debts. *Brown v. New Bedford Inst. for Sav.* 137 Mass. 262 (1884).

⁶ *Vaupell v. Woodward*, 2 Sandf. Ch. 143 (1844). The pledge may be made to secure the carrying out of a contract and a court of equity will foreclose it al-

an intent to sell the stock, and may so sell it, without any judicial proceedings, and apply the proceeds to the payment of the debt.¹ No express power to sell need be contained in the memorandum of pledge in order to authorize the latter remedy. It exists by force of law.

The pledgee, however, is not bound to pursue either remedy, merely because the debt is due and unpaid.² He need not sell the stock upon the maturity of the note secured, nor is he liable because the stock declines in value. He may sue on the debt without tendering back the stock.³ The pledgor cannot compel him to sell by merely giving him notice so to do.⁴ Nor is the pledgee bound to sell on non-payment of the debt, although the memorandum of pledge expressly authorizes a sale, but he may file a bill in equity to foreclose instead of pursuing the other remedy.⁵ The pledgee's remedy as a pledgee is never by attaching the stock and selling it at an execution sale.⁶ In pursuing such a pro-

though the damages are unliquidated. *Robinson v. Hurley*, 11 Iowa, 410, from which it seems that where the pledge was made without a written transfer of the certificate this is the only remedy. See also *Merchants Nat'l Bk. v. Hall*, 83 N. Y. 338 (1881); *Smith v. Coale*, 34 Leg. Int. 58; *Blouin v. Liquidators, &c.*, 30 La. Ann. 714 (1878); *Briggs v. Oliver*, 68 N. Y. 336; *Johnson v. Dexter*, 2 McArthur, 530.

¹ Story on Bailments, 9th ed. (1877) § 310, saying: "The law as at present established leaves an election to the pawnee. He may fill a bill in equity against the pawnor for a foreclosure and sale; or he may proceed to sell *ex mero motu*, upon giving due notice of his intention to the pledgor. In the latter case, if the sale is *bona fide* and reasonably made, it will be equally obligatory as in the first case." The leading case, allowing this remedy of the pledgee against the pledge, is *Tucker v. Wilson*, 5 Bro. Par. Cases, 193 (1714), rev'g 1 P. Wms. 261. In *Brown v. Ward*, 3 Duer, 660 (1854), the court says: "Since the time of the case of *Hart v. Ten Eyck* [2 Johns. Ch. Cas. 180], before Chancellor Kent, the right of the pledgee to sell after the debt is due, upon reasonable notice, has been unquestioned, and a custom has grown up and has been sanctioned by the courts of selling stocks at the Merchants Exchange." To same effect, *Diller v. Brubaker*, 52 Penn. St. 498 (1866); *Finney's Appeal*, 59 Penn. St. 398 (1868);

Mount Holly, &c., Co. v. Ferree, 17 N. J. Eq. 117 (1864), where the court says, "A sale of a pledge by the pawnee where reasonably and *bona fide* made, and after notice to the pawnor, is equally obligatory as if made by judicial process." 2 Kent's Com. 582, saying that the pledgee "may file a bill in chancery and have a judicial sale under a regular decree of foreclosure . . . and he may sell without judicial process, upon giving reasonable notice to the debtor to redeem." *Stearns v. Marsh*, 4 Denio, 227 (1847); *Markham v. Jaudon*, 41 N. Y. 235, 241 (1869). The parties may provide for any manner of disposing of the pledge to satisfy the claim upon it, which is not in contravention of statute, against public policy or fraudulent. *McNeil v. Tenth Nat'l Bk.*, 46 N. Y. 325, 334, says: "The distinction between a lien and a pledge is said to be that a mere lien cannot be enforced by sale by the act of the party, but that a pledge is a lien with a power of sale superadded."

² *O'Neil v. Whigham*, 87 Penn. St. 394 (1878); *Rezet v. McClellan*, 48 Ill. 345 (1868).

³ *Taylor v. Cheever*, 6 Gray, 146.

⁴ See § 476.

⁵ *Cornick v. Richards*, 3 Lea (Tenn.), 1 (1879); *Coffin v. Chicago & N., &c., Co.*, 4 Hun, 625 (1875).

⁶ *Lee v. Citizen's Nat'l Bk.*, 2 Cin. Super. Ct. 298 (1872). It seems, however, that his remedies as a pledgee are not af-

cedure, he abandons his character as pledgee, and retains that of creditor only.

§ 477. *Notice of sale of stock by pledgee to apply to debt secured.*—In case the pledgee pursues the remedy of selling the stock, without any judicial proceedings, he must give the pledgor reasonable notice of the intent to sell and of the time and place of sale.¹ A sale without a notice is a conversion of the stock.² The pledgee must demand payment of the debt secured by the pledge of stock, and a waiver of notice of sale is not a waiver of a right to have such a demand made.³ A notice of intent to sell, however, is equivalent to a demand of payment.⁴ A broker's custom to the effect that no notice is necessary is illegal and void.⁵ The time and place of the proposed sale must be specified in the notice.⁶ The time between the service of the notice and the time when the sale is to take place must be reasonable in length, so as to give the debtor an opportunity to obtain money to pay the debt.⁷ In Massachusetts, by statute, sixty days' notice must be

fectured by his pursuit of other remedies. See *Hill v. Beebe*, 18 N. Y. 556, 563, 567.

¹ "To authorize the defendants to sell the stock purchased, they were bound, first, to call upon the plaintiff to make good his margin; and, failing in that, he was entitled, secondly, to notice of the time and place where the stock would be sold; which time and place, thirdly, must be reasonable." *Markham v. Jaudon*, 41 N. Y. 235, 243 (1869). See also *Stratford v. Jones*, 97 N. Y. 586 (1885); *Baker v. Drake*, 66 N. Y. 518 (1876); *Conyngham's Appeal*, 57 Penn. St. 474; *Stearns v. Marsh*, 4 Denio, 227; *Neiler v. Kelley*, 69 Penn. St. 403; *Cushman v. Hayes*, 46 Ill. 145. A joint owner is entitled to notice. *Clark v. Sparhawk*, 2 Weekly Notes, 115.

² *Fowle v. Ward*, 113 Mass. 548 (1873); *Hempling v. Burr*, 26 Northwest. Rep. 496 (Mich., 1886).

³ *Lewis v. Graham*, 4 Abb. Pr. 106 (1857); *Brass v. Worth*, 40 Barb. 59 (1863); *Wilson v. Little*, 2 N. Y. 443, 448 (1849), saying: "It is well settled that where no time is expressly fixed by contract between the parties for the payment of a debt secured by a pledge, the pawnee cannot sell the pledge without a previous demand of payment, although the debt is technically due immediately." *Genet v. Howland*, 45 Barb. 560 (1866).

⁴ *Nabring v. Bk. of Mobile*, 58 Ala. 204 (1877). So also of notice of intent to foreclose. *Howe v. Bemis*, 2 Gray, 208.

⁵ *Markham v. Jaudon*, 41 N. Y. 235 (1869).

⁶ *Conyngham's Appeal*, 57 Penn. St. 474 (1868); *Genet v. Howland*, *supra*; *Canfield v. Minn., &c., Assn.*, 14 Fed. Rep. 801. See *Schouler on Bailments*, 206-212. It has been held in Maryland that a notice of the place is unnecessary. *Worthington v. Tormey*, 34 Md. 182. But such a decision would be unsafe, and probably would not be followed elsewhere. In New York, the place of sale formerly, by custom, was at the Merchants' Exchange, No. 111 Broadway, but is now at the Real Estate Exchange in Liberty Street.

⁷ In Maryland, &c., *Co. v. Dalrymple*, 25 Md. 242, a week's notice was held sufficient. *Lewis v. Graham*, 4 Abb. Pr. 106 (1857), holding that 34 days, where the pledgor resides in Illinois and the sale is to be in New York, is sufficient. *Bryan v. Baldwin*, 7 Lons. 174 (1872); *aff'd*, 52 N. Y. 232, holding that two days was sufficient. *Stevens v. Hurlbut Bk.*, 31 Conn. 146 (1862), holding that a sale on the same day is unreasonable and the notice insufficient. See other cases in Chapter XXV, § 458; *Willoughby v. Cornstock*, 3 Hill, 389 (1842), where two

given.¹ A notice by a newspaper advertisement is insufficient.² It must be served personally, and it seems that it cannot be served on one who has charge of the pledgor's office for the transaction of business.³ By an express agreement the pledgor may waive his right to a notice of the time and place of the sale.⁴ Such contracts are frequently entered into with stock-brokers by customers buying stock on a margin. But an express power to the pledgee to sell the pledge on certain contingencies is not a waiver of a right to notice.⁵

§ 478. *Formalities of sale.*—A sale of stock on notice by a pledgee, for the purpose of applying the proceeds to the pledgor's debt, must be at public auction.⁶ A private sale is unauthorized and illegal, even though the utmost market price is obtained.⁷ The pledgee cannot have the sale made at a broker's board or in a Stock Exchange, since only the members of the association are allowed to bid for stocks sold therein, while the law requires that the public shall be allowed to bid at a pledgee's sale.⁸ Frequently a special agreement is made between the pledgor and pledgee, especially between a customer and his stock-broker, whereby the pledgee is allowed to sell at a broker's board.⁹ Such an agreement, however, does not authorize a private sale at the broker's board.¹⁰

days was held sufficient. *Edwards on Bailments*, 285. As to place of sale, see Chapter XXV, § 458 and § 476.

¹ Gen. Stat. c. 151, § 9.

² *Lewis v. Graham*, *supra*; and see § 119.

³ *Bryan v. Baldwin*, 52 N. Y. 232 (1873). *Cf. Milliken v. Dehon*, 27 N. Y. 364 (1863).

⁴ *Maryland Fire Ins. Co. v. Dalrymple*, 25 Md. 242 (1866); *Genet v. Howland*, *supra*; and see Ch. XXV, §§ 459, 462; *Milliken v. Dehon*, 27 N. Y. 364; *Stevens v. Hurlbut Bk.*, 31 Conn. 146; *Hyatt v. Argenti*, 3 Cal. 151; *Wheeler v. Newbould*, 16 N. Y. 392; *Stenton v. Jerome*, 54 N. Y. 480; *Wicks v. Hatch*, 62 N. Y. 535. Formerly the validity of a waiver was doubted. *Campbell v. Parker*, 9 Bosw. 322; *Wilson v. Little*, 2 N. Y. 443, 448; *Gilpin v. Howell*, 5 Penn. 41; *Hanks v. Drake*, 40 Barb. 186; *Sterling v. Jaudon*, 48 Id. 459.

⁵ *Stevens v. Hurlbut Bk.*, 31 Conn. 146 (1862). *Cf. Milliken v. Dehon*, 27 N. Y. 364 (1863). But an express power to sell on a specified day is held to waive right

of notice. *Bryson v. Raynor*, 25 Md. 424 (1866).

⁶ *Conyngham's Appeal*, 57 Penn. St. 474 (1868); *Rankin v. McCullough*, 12 Barb. 103 (1851); *Genet v. Howland*, 45 Barb. 560 (1866); *Ogden v. Lathrop*, 65 N. Y. 158 (1875). An express power to sell has been held to authorize a private sale. *Bryson v. Raynor*, 25 Md. 424 (1866). Or a sale at a broker's board.

⁷ *Castello v. City Bk. of Albany*, 1 Leg. Obs. 25 (1842); *Willoughby v. Comstock*, 3 Hill, 389 (1842). *Cf. Nabring v. Bk. of Mobile*, 58 Ala. 205 (1877). The pledgee's right to object is waived by long delay. *Hayward v. Natl. Bk.*, 96 U. S. 611 (1877).

⁸ *Brass v. Worth*, 40 Barb. 648 (1863); *Rankins v. McCullough*, 12 Barb. 103 (1851).

⁹ *Wicks v. Hatch*, 62 N. Y. 535 (1875). In Maryland a contrary rule prevails. *Maryland Fire Ins. Co. v. Dalrymple*, 25 Md. 242 (1866). See Ch. XXV.

¹⁰ *Allen v. Dykers*, 3 Hill, 593; 7 Id. 497.

§ 479. *Pledgee himself cannot purchase at the sale.*—It is a well established rule that where a pledgee pursues the remedy of selling the stock upon notice, the pledgee himself is disqualified from purchasing the stock.¹ This rule is based on the principle that the law carefully protects the interest of the pledgor, and will not open the door to possible devices of the pledgee for purchasing the stock for himself at a low price. The pledgee cannot purchase either directly or indirectly, in his own name or in the name of another. The effect of a purchase by the pledgee for himself is that the whole proceeding of the pledgee for subjecting the pledge to the payment of the debt is utterly futile, and voidable at the election of the pledgor. The pledgor cannot claim that the pledgee has converted the stock by purchasing at the sale,² but he may disregard the notice and sale and whole proceeding as being ineffectual and voidable. The pledge relationship continues as though no attempt had been made by the pledgee to subject the pledge to the payment of the debt.³ Where, however, the pledge is foreclosed by legal proceedings similar to those for the foreclosure of chattel mortgages, it seems to be in the power of the court to insert in the decree a provision allowing the pledgee to purchase on the sale.

¹ *Bryan v. Baldwin*, 52 N. Y. 232 (1873), the court saying: "The plaintiff being the pledgee of the stock, and in that character exposing it for sale, could not become the purchaser unless the defendant assented to such purchase. This sale to the plaintiff was not void, but voidable, at the election of the defendant." *Maryland Fire Ins. Co. v. Dalrymple*, 25 Md. 242 (1866). Nor can he buy where the pledge is being sold on a forfeiture sale for non-payment of calls. *Freeman v. Harwood*, 49 Me. 195 (1859). The pledgor's silence may constitute a ratification of the pledgee's purchase. *Carroll v.*

Mullanphy Sav. Bk., 8 Mo. App. 249 (1880). If the pledgee is a corporation, its president cannot purchase for it. *Star Fire Ins. Co. v. Palmer*, 41 Super. Ct. 267 (1876); *Lewis v. Graham*, 4 Abb. Pr. 106 (1857), holds that a special partner of the pledgee firm may purchase. And see Chap. XXV, § 450. *Of. Finney's Appeal*, 59 Penn. St. 398 (1868).

² *Bryan v. Baldwin*, 52 N. Y. 232 (1873).

³ *Bryson v. Raynor*, 25 Md. 424 (1866); *Middlesex Bk. v. Minot*, 45 Mass. 325 (1842); *Hestonville, &c., R. R. Co. v. Shields*, 3 Brews. (Penn.) 257 (1869).

CHAPTER XXVII.

LEVY OF ATTACHMENT AND EXECUTION UPON SHARES OF STOCK.

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| <p>§ 480. An execution at common law could not reach shares of stock.</p> <p>481. Nor, it seems, could a court of equity subject stock to the payment of debts.</p> <p>482. By statutory provisions, executions are generally sufficient to reach the debtor's stock.</p> <p>483. Attachment of stock as allowed by the statutes of the various States.</p> <p>484. Attachment of pledge, &c., and of stock which the debtor has fraudulently transferred away.</p> <p>485. Stock can be attached only in the State creating the corporation.</p> <p>486. Rights of an unregistered transferee of a certificate of stock as</p> | <p>against an attachment or execution levied on that stock.</p> <p>§ 487. Rule in New York, Pennsylvania, New Jersey, South Carolina, Texas, Louisiana, and the Federal Courts.</p> <p>488. Rights and duties of the corporation in such cases.</p> <p>489. Rule in Connecticut, Maine, New Hampshire, Vermont, Indiana, Illinois, Wisconsin, and California.</p> <p>490. Rule in Massachusetts.</p> <p>491. Shares of stock cannot be subjected to the payment of the stockholder's debts by the process of garnishment.</p> |
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§ 480. *An execution at common law could not reach shares of stock.*—A share of stock is in the nature of a chose in action, and at common law a chose in action could not be reached by or made subject to a levy of execution. Consequently it has been uniformly held by the courts that at common law a levy of execution could not be made on shares of stock. Unless, therefore, the process of execution has been extended by statute, so as to reach such property, the stock of a judgment-debtor cannot be subject to the payment of his debts by means of an execution.¹ An attachment, being entirely statutory, can be levied on shares

¹ Van Norman v. Jackson County Circuit Judge, 45 Mich. 204 (1881); Goss v. Phillips, &c., Co., 4 Bradw. 510 (1879); Blair v. Compton, 33 Mich. 414 (1876); Slaymaker v. Bank of Gettysburg, 10 Penn. St. 373 (1849); Foster v. Potter, 37 Mo. 525 (1866); Howe v. Starkweather, 17 Mass. 240 (1821); Nabring v. Bk. of Mobile, 58 Ala. 204 (1877); Denton v. Livingston, 9 Johns. 96 (1812), per Chancellor Kent; Nashville Bk. v. Ragsdale, Peck (Tenn.), 296 (1823). Even where

the stock is held to be real estate. Cooper v. Canal Co., 2 Murph. (N. C.) 195 (1812). Cf. Gue v. Tidewater Canal Co., 24 How. (U. S.) 257 (1860). At an early day, when the nature of stock was little understood, an attachment was attempted on the corporate property for the debts of a stockholder. It failed. Williamson v. Smoot, 7 Mart. (La.) 81 (1819). Stock cannot be taken on a tax warrant. Barnes v. Hall, 55 Vt. Rep. 420.

of stock only when the words of the statute declare that an attachment may be levied on such property.¹

§ 481. *Nor, it seems, could a court of equity subject stock to the payment of debts.*—There is some doubt whether a court of equity has power to subject a judgment-debtor's choses in action to the payment of his debts, where the only ground for the interference of the court is that unless it does interfere, such property cannot be reached by the judgment-creditor. In New York, previous to the statutes regulating this subject, the jurisdiction of a court of equity herein, was emphatically denied in one case,² and with equal emphasis declared to exist in another case.³ The English authorities are quite uniform in holding that a court of equity has no such jurisdiction.⁴ And in America, for the most part, a similar conclusion is arrived at.⁵ Where, however, the debtor has conveyed away his stock, for the purpose of defrauding his creditors, a court of equity will aid the judgment-creditor, inasmuch as it has jurisdiction in all matters involving fraud, trust, or accident, or other ingredient of similar character.⁶

§ 482. *By statutory provisions, executions are generally sufficient to reach the debtor's stock.*—Nearly all of the States of the Union have enacted statutes extending the scope of executions, so as to render subject to them, all choses in action, including shares of stock in a corporation. Frequently special provisions are made applicable to stock and prescribing the steps

¹ *Plimpton v. Bigelow*, 93 N. Y. 592, 602 (1883); *Merchants Mut. Ins. Co. v. Brower*, 38 Texas, 230 (1873).

² *Donovan v. Finn*, Hopk. Ch. 67, 91 (1823).

³ *Storm v. Waddell*, 2 Sand. Ch. 495, 511 (1845).

⁴ *Dundas v. Dutens*, 1 Ves. 196 (1790); *Bk. of Eng. v. Lunn*, 15 Ves. 569 (1809); *Grogan v. Cooke*, 2 Ball & B. (Ir. Ch.) 230 (1812); *Nantes v. Corrock*, 9 Ves. 183 (1803); *McCarthy v. Gould*, 1 Ball & B. (Ir. Ch.) 387 (1810), applying the same rule to dividends. In *King v. Dupine*, 2 Atk. 603, note (1744), a court of equity subjected to the payment of a debt the debtor's reversionary interest in an annuity. In *Horn v. Horn*, Amb. 79 (1749), the court refused aid, inasmuch as the debtor had been imprisoned under a *cap. satis*.

⁵ *Williams v. Reynolds*, 7 Ind. 622 (1856); *Disborough v. Outealt*, Saxton's Ch. (N. J.) 298, 306 (1831); *McFerran v. Jones*, 2 Litt. (Ky.) 219 (1822); *Erwin v. Oldman*, 6 Yerg. 185 (1834). *Contra, dictum*, *Watkins v. Dorsett*, 1 Bland's Ch. 530 (1828). In *Brightwell v. Mallory*, 10 Yerg. (Tenn.) 198 (1836), the proceeding was statutory.

⁶ See §§ 339, 340, on Statute of Frauds; also *Taylor v. Jones*, 2 Atk. 600 (1743), holding that the debtor's transfer of stock in trust was in fraud of creditors. *Hadden v. Spader*, 20 Johns. (N. Y.) 554 (1822); *Scott v. Indianapolis Wagon Works*, 48 Ind. 75 (1874); *Van Norman v. Jackson Circuit Judge*, 45 Mich. 204 (1881); *Lathrop v. McBurney*, 71 Ga. 815 (1883).

which are necessary in rendering the execution levy effectual. Where an execution is levied in accordance with such statutes, its provisions must be substantially complied with, and if not complied with, the sale is not merely voidable, but is wholly unauthorized and void.¹ It is fatal to the levy and sale, if the sheriff fails to give to the corporation the notice as is generally required by statute;² or if the sale by the sheriff is not made promptly, as advertised in accordance with the statute.³ The sale itself is not complete until the sheriff gives the proper instruments of title to the purchaser, and until then the corporation is not obliged to recognize the latter as having any rights.⁴ Whether or not an execution can be levied on stock which has been fraudulently transferred away by the judgment-debtor, depends upon the wording of the statute allowing the levy of execution on stock. If it allows a levy on all interests of the debtor, whether legal or equitable, then the fraudulent transfer may be disregarded, and the stock seized as though still standing in the name of the judgment-debtor.⁵ If, however, the statute does not expressly provide 'for a levy on an equitable interest, the judgment-creditor's remedy is not an execution, but a suit in equity

¹ *Blair v. Compton*, 33 Mich. 414 (1876), holding that where the sheriff sold without knowing or stating how many shares of stock the debtor owned, and which were being sold, that the sale was void. See also *People v. Goss, &c., Mfg. Co.*, 99 Ill. 355 (1881), reversing *Goss, &c., Mfg. Co. v. People*, 4 Bradw. 510, the court saying, that in Illinois an actual levy upon shares of stock held by a debtor in a corporation is accomplished by the sheriff, when he has exhibited to the keeper of the stock books of the corporation his execution, and on demand, for the purpose of the levy, has procured and received from the corporation "a certificate of the number of shares or amount of interest held by the judgment-debtor," and has indorsed upon his execution a statement that the shares named in the certificates are taken in execution, or levied upon. When the sheriff delivers to the proper officer of the corporation an attested copy of the execution, the stock of the debtor is considered as seized on execution, this being a constructive levy. The procedure in levy of execution on stock, as laid down by the charter of the corporation, supersedes the procedure of a

previous general statute. *Titcomb v. Union Marine, &c., Ins. Co.*, 8 Mass. 326 (1811). And *vice versa*, *Howe v. Starkweather*, 17 Mass. 240 (1821). The sheriff need not sell the stock in parcels, but may sell the whole at once. *Morris v. Conn. &c., R. R. Co.* (Montreal Ct. of Appeals, September, 1886).

² *Princeton Bk. v. Crozer*, 22 N. J. Law, 383 (1850), where no notice was given, but the stock was merely mentioned in the inventory returned by the sheriff.

³ *Titcomb v. Union Marine, &c., Ins. Co.*, 8 Mass. 326 (1811), and *Howe v. Starkweather*, 17 Mass. 240 (1821), where the sale was made after the proper day, without a re-advertisement, and consequently was held to be void. The court said, "The sale of them upon execution not being justifiable at common law, the statute must be strictly pursued to give any property to the purchaser."

⁴ *Morgan v. Thames Bk.*, 14 Conn. 99 (1840).

⁵ *Scott v. Indianapolis Wagon Works*, 48 Ind. 75 (1874). Cf. *State v. Warren Foundry, &c., Co.*, 32 N. J. L. 439 (1868).

to set aside the fraudulent transfer.¹ If the statute prescribes that the corporation shall register as a stockholder the purchaser at the execution sale, the writ of *mandamus* will lie to compel the corporation to make such registry,² but the relator must allege that he presented to the corporation the required papers, and was refused such registry.³

§ 483. *Attachment of stock as allowed by the statutes of the various States.*—The States of the Union have quite generally passed statutes providing for the attachment of a debtor's property where the debtor is a non-resident, or is guilty of a fraud, or where other facts exist which bring the case within the attachment statute. Inasmuch, as in modern times, a large part of the property of individuals consists of shares of stock in corporations, the attachment statutes generally provide specially for the attachment of stock, and give specific directions in reference to the steps necessary to be taken in making such attachment.⁴ In New York an attachment of stock is provided for, but an execution without a previous attachment is not allowed.⁵ It has been held

¹ Van Norman v. Jackson County Circuit Judge, 45 Mich. 204 (1881).

² Bailey v. Strohecker, 38 Ga. 259 (1868). See also § 390.

³ Lippett v. American Wood Paper Co., 14 R. I. 301 (1883).

⁴ Cal., Code of C. Proc. § 5141; Colorado, Code of C. Proc. § 97; Conn., Gen. Stat. (1875), § 6; Ga., Code of 1882, §§ 3289-3291; Ind., R. S. (1881), § 933; Iowa (McClain's Annotated Stat. 1880), § 2967; Maine, R. S. 1884, ch. 81, § 27; Md., R. Code of 1874, § 20; Mass., Public Stat. 1882, ch. 161, §§ 71-73; Mich. (Howell's Annotated Stat. 1883); Minn., Gen. Stat. 1878, § 156; Mo., R. S. 1879, § 417; Neb., Com. Laws 1881, ch. 3, § 201; Nev., Gen. Stat. 1885, ch. 4, §§ 3149, 3150; New Hampshire, Gen. L. 1878, ch. 224, § 13; N. Y., Code of Civil Proc., § 647; also § 649, as amd. by L. 1879, ch. 541, also §§ 650, 651, 708 (2); Ohio, R. S. 1880, title 1, div. 6, ch. 2, § 5524; Penn., Brightley's P. Dig., § 71; S. C., Code of C. Proc., ch. 4, §§ 256-258; Wis., R. S. 1878, § 2738. Where both an attachment and an execution on stock is allowed by statute, the former is said to be the preferable remedy when the corporation has a lien on the stock, or there is a claimant to the stock. Weaver

v. Huntingdon, &c., Coal Co., 50 Penn. St. 314 (1865); Lex v. Potters, 16 Penn. St. 295 (1851). In New York shares of stock cannot be levied on under a writ of execution, although they may be attached and subsequently sold by execution in that suit. Code of Civil Procedure, §§ 649-651. See 4 Wait's Pr. 36, J. Stock may be reached, however, by proceedings supplementary to execution. See in general, Barnes v. Morgan, 3 Hun. 703. Under the English statutes, 1 & 2 Vict., c. 110, § 14, and 3 & 4 Vict., c. 82, § 1, stock in any public company standing in the name of any person against whom judgment shall have been obtained, whether "in his own right or in the name of any person in trust for him," may be charged by a judge's order with the payment of the amount of the judgment. The statute says: "The interest of any judgment-debtor, whether in possession, remainder, or reversion, and whether vested or contingent," may be so reached. Cragg v. Taylor, L. R., 2 Ex. 131 (1867); Baker v. Tynte, 2 Ell. & E. 897 (1860).

⁵ O'Brien v. Mechanics & T. Ins. Co., 56 N. Y. 52 (1874); Smoot v. Heim, 1 Civ. Proc. Rep. 208 (1881), are cases arising under the attachment law.

that shares of stock may be attached under the general provisions of an attachment law, which does not specify shares of stock as being subject to an attachment.¹ The formalities prescribed by the statute must be complied with fully, as in the case of a levy of execution upon stock.²

§ 484. *Attachment of pledge, &c., and of stock which the debtor has fraudulently transferred away.*—As has been said in the case of an execution levied on shares of stock, an attachment may be levied on the same, when the words of the attachment statute are so broad as to render subject to the attachment, all equitable interests of the debtor whose stock is attached. Thus it has been held in Ohio and New Jersey, that where the debtor has transferred away his stock, for the purpose of defrauding his creditors, an attachment of the stock will lie nevertheless.³ An attachment may be levied upon stock although the stock has been mortgaged or pledged, and the attaching creditor is seeking to reach merely the equity of redemption.⁴ An attachment is not the proper remedy for a pledgee who wishes to subject the pledge

¹ *Chesapeake & O. R. R. Co. v. Paine*, 29 Gratt. (Va.) 502 (1877), where stock was held to be included under the word "estate," and the procedure prescribed for garnishment was followed and upheld. So also *Curtis v. Steever*, 36 N. J. L. R. 304 (1873), where an attachment of stock was upheld, though the statute merely allowed attachment of "rights and credits." In *Haley v. Reid*, 16 Ga. 437 (1854), however, an attachment of stock was not allowed where the statute allowed levy "upon the estate, both real and personal." See also *Merchants M. Ins. Co. v. Brower*, 38 Texas, 230 (1873). It has been held that there can be no attachment of stock under a statute which allows an attachment of "real and personal property." *Foster v. Potter*, 37 Mo. 525.

² *Stamford Bk. v. Ferris*, 17 Conn. 259 (1845), where the attachment failed, because the sheriff did not leave a copy of the writ duly indorsed, with the corporation, even though the cashier of the corporation was absent. A transfer subsequent to such irregular attachment is valid and carries title.

³ *Natl. Bk. of N. L. v. Lake Shore & M. S. R. R. Co.*, 21 O. St. 221 (1871), holding also that the attachment is good,

even though the corporation deny that the defendant owns any stock therein. *Curtis v. Steever*, 36 N. J. L. Rep. 304 (1873), the court saying that the attachment is good, since the fraudulent transfer is void, and holding that the transferee may bring a suit for trespass, and that the attaching creditor may then set up the fraud in defense. *Cf. State v. Warren Foundry, &c., Co.*, 32 N. J. L. 439 (1868).

⁴ *Edwards v. Beugnot*, 7 Cal. 162 (1857), holding also that if the mortgage is recorded on the corporate books, notice must be served on the mortgagee also, and that where one attachment was served on the corporation, and another on the mortgagee, that the latter attachment prevails and takes the surplus. *Norton v. Norton* (Ohio, Nov., 1885), holding that the court will order the stock to be sold, the pledgee paid and the balance held under the attachment. A garnishment for the surplus is ineffectual. *Kyle v. Montgomery*, 73 Ga. 337 (1884); *Seeligson v. Brown*, 61 Texas, 114 (1884); *Mechanics, &c., Assn. v. Conover*, 14 N. J. Eq. 219 (1862); *Foster v. Potter*, 37 Mo. 525; *Manns v. Brookville Natl. Bk.*, 73 Ind. 243 (1881); *Nabring v. Bk. of Mobile*, 58 Ala. 204 (1877).

to the payment of the debt.¹ His remedy is by foreclosure or a public sale on notice to the pledgor. Dividends on the stock which is attached follow the stock, and are covered by the attachment.² An attachment will lie in Rhode Island, for stock which is registered in the name of a person other than the defendant, the transfer by the defendant having been in fraud of creditors.³ Where the corporation has a lien on stock for debts due from the stockholder to the corporation, it may enforce the lien by an attachment.⁴

§ 485. *Stock can be attached only in the State creating the corporation.*—Shares of stock in a corporation are personal property, whose location is in the State where the corporation is created.⁵ It is true, that for purposes of taxation and some other similar purposes, stock follows the domicile of its owner, but considered as property separated from its owner, stock is in existence only in the State of the corporation. All attachment statutes provide for the attachment of a non-resident debtor's property in the State, and generally, under such statutes, the stock owned by a non-resident in a corporation created by the State wherein the suit is brought, may be attached and jurisdiction be thereby acquired to the extent of the value of the stock attached.⁶ But under no circumstances can an attachment be levied on a defendant's shares of stock, in an action commenced outside of the State wherein the corporation is incorporated. For purposes of attachment, stock is located where the corporation is incorporated, and nowhere else.⁷ The shares owned by a non-resident defendant in the stock of a foreign corporation, cannot be reached and levied upon by virtue of an attachment, although officers of the corporation are within the State engaged in carrying on the corporate business.⁸ Nor can

¹ Lee v. Citizens Natl. Bk., 2 Cin. Super. Ct. 298, 312 (1872).

² Moore v. Gennett, 2 Tenn. Ch. 375 (1875).

³ Beckwith v. Burroughs, 14 R. I. 366 (1884). And the purchaser at the execution sale may file a bill in equity to clear the title to the stock. *Of. Id.*, 13 R. I. 294 (1881).

⁴ Sabin v. Bk. of Woodstock, 21 Vt. 353 (1849).

⁵ Evans v. Monet, 4 Jones' Eq. (N. C.) 227 (1858).

⁶ Natl. Bk. of N. L. v. Lake Shore &

M. S. R. R. Co., 21 O. St. 221 (1871); Chesapeake & O. R. R. Co. v. Paine, 29 Gratt. (Va.) 502 (1877).

⁷ Winslow v. Fletcher, 13 Am. & Eng. Corp. Cas. 39 (Conn., 1886), the court saying that "stock in a corporation for the purposes of an attachment, has its *situs* where the corporation is located."

⁸ Plimpton v. Bigelow, 93 N. Y. 592 (1883), the court saying: "We do not doubt that shares for the purpose of attachment proceedings may be deemed to be in the possession of the corporation which issued them, but only at the place

such an attachment be levied although the foreign corporation has a branch registry office in the State where the attachment is levied, and although the certificates of stock are also in such State.¹ Certificates of stock are not the stock itself. They are but evidence of the stock, and the stock itself cannot be attached by a levy of attachment on the certificate.² As was well said by the Supreme Court of Pennsylvania, stock cannot be attached by attaching the certificate, any more than lands, situated in another State can be attached by an attachment in Pennsylvania levied on the title deeds to such land.³ There can be no attachment of stock as the property of an unregistered holder, through whom title has passed to another.⁴

§ 486. *Rights of an unregistered transferee of a certificate of stock as against an attachment or execution levied on that stock.*—The most difficult and unsettled question connected with an attachment or execution levied on stock, is the question of how far a purchaser of the certificate of stock from the stockholder and debtor is protected in his ownership, where such purchaser does not have his transfer registered on the corporate books, before the attachment or execution is levied. This question is especially important, since it affects the rights of a *bona fide* purchaser of stock in the open market, and constitutes one of the

where the corporation by intendment of law always remains, to wit, in the State or country of its creation. . . Manifestly the *res* cannot be within the jurisdiction, as a mere consequence of a legislative declaration, when the actual locality is undeniably elsewhere." Garnishment proceedings also will not apply. The defendant may move to have the attachment levy set aside. *Martin v. Mobile & O. R. R. Co.*, 7 Bush (Ky.), 116 (1870), holds that a statute authorizing a foreign corporation to exercise certain powers does not make it a domestic corporation.

¹ *Christmas v. Biddle*, 18 Penn. St. 223 (1850), approved in *Childs v. Digby*, 24 Penn. St. 23 (1854). In this case the attachment was levied in Pennsylvania on certificates of stock in Pennsylvania, but belonging to a citizen of Mississippi, and the corporation was created by the laws of Mississippi.

² *Christmas v. Biddle*, *supra*; *Moore v. Gennett*, 2 Tenn. Ch. 375 (1875).

³ *Christmas v. Biddle*, *supra*. In

Winslow v. Fletcher, 13 Am. & Eng. Corp. Cas. 39 (Conn., 1886), the court well says: "While the certificates are in themselves valuable for some purposes, and to some extent may properly be regarded as property, yet they are distinct from the holders' interest in the capital stock of the corporation, and are not goods and effects within the meaning of the statute relating to foreign attachment. They are no more subject to an attachment or a trustee process than a promissory note. The debt is subject to attachment, but the note itself, which is simply evidence of the debt, is not. So with stock. That may be attached, but the certificate cannot be."

⁴ *Lippett v. American, &c., Co.*, 1 East. Rep. 487 (R. I., 1885). Thus, where A, the registered stockholder, transfers the certificate of stock to B, and B transfers it to C, and C obtains registry directly from A, there can be no attachment of the stock against B.

greatest dangers incurred in the purchase of certificates of stock. On one point, it seems that the courts of all the States agree. If a stockholder, whose stock has been already attached or sold on execution, sells his certificate of stock, after the levy of such attachment or execution, the vendee or transferee buys subject to such levy, even though he had no knowledge of it. The stock, in contemplation of law, has already been seized by the levy, and the purchaser is bound to take notice of that fact.¹ The only means of avoiding this danger in the purchase of stock, is by an inquiry at the office of the corporation, at the time of making the purchase. A different question presents itself, when the stockholder against whose stock an attachment or execution is levied, has already and before such levy sold and transferred his certificate of stock, but that transfer has not been registered on the corporate books. The courts of the different States are in irreconcilable conflict on this question of whether the unregistered transferee is protected in his purchase.

§ 487. *Rule in New York, Pennsylvania, New Jersey, South Carolina, Texas, Louisiana, and the Federal Courts.*—The decided weight of authority holds, that he who purchases for a valuable consideration, a certificate of stock, is protected in his ownership of the stock, and is not affected by a subsequent attachment or execution levied on such stock, for the debts of the registered stockholder, even though such purchaser has neglected to have his transfer registered on the corporate books, thereby allowing his transferrer to appear to be the owner of the stock upon which the attachment or execution is levied. Such is the rule prevailing in the Federal courts, and in the courts of the above named States.² Frequently this rule is justified and ex-

¹ *Chesapeake & O. R. R. Co. v. Paine*, 29 Gratt. (Va.) 502 (1877); *Shenandoah Valley R. R. Co. v. Griffith*, 76 Va. 913.

² The case of *Smith v. American Coal Co.*, 7 Lans. 317 (1873), fully discusses and sustains this rule. See also *Comeau v. Guild Farm Oil Co.*, 3 Daly, 218 (1870), where Van Brunt, J., says that the sheriff, "by the levy of such an attachment, could not acquire any better or greater title to the stock, than a person would have done who had purchased this stock of the person in whose name it stood on the day of the levy of the attach-

ment. And the principle is well established in this State, that such a purchaser would not acquire any interest whatever, as against a prior purchaser for value." For Pennsylvania, see *Eby v. Guest*, 94 Penn. St. 160 (1880); *Finney's Appeal*, 59 Penn. St. 398 (1868); *Commonwealth v. Watmouth*, 6 Whart. 117 (1840), holding also that the sheriff need not levy on stock which he knows has already been sold to an unregistered transferee. *United States v. Vaughan*, 3 Binn. 394 (1811), where the unregistered transferees resided in foreign lands. See also, for other

plained, on the ground that registry, and by-laws or charter provisions requiring registry of transfers on the corporate books, are not for the purpose of notifying the creditors of the old registered stockholder that he no longer owns the stock, nor for any similar purpose, but are for the purpose of protecting the corporation in paying dividends, and allowing the stock to be voted. Another and stronger reason is that the law favors the transfer of stock certificates, and decreases, so far as possible, all secret dangers incurred in its purchase.

By protecting the purchaser against subsequent attachments and executions, the law removes one of the chief risks incurred by holding certificates of stock without a registry, and thereby increases the safety and desirability of such investments. If the corporation improperly refuses to allow the transferee of stock to register his transfer, and the stock is afterwards attached by a creditor of the old stockholder, the transferee may, if he chooses, hold the corporation liable in damages for its refusal to allow the registry.¹

§ 488. *Rights and duties of the corporation in such cases.*—The corporation has a dangerous duty to perform when stock has been attached or sold under levy of execution, and a registry is requested by the purchaser at such sale, or by a purchaser of the outstanding certificate of stock. If the purchaser of the certificate demands registry, before registry has been allowed to the pur-

States, *Broadway Bank v. McElrath*, 18 N. J. Eq. 24 (1860); s. o. *sub nom.* *Hunterdon Bk. v. Nassau Bk.*, 2 C. E. Gr. 496; *Rogers v. Stevens*, 8 N. J. Eq. 167 (1849); *Fraser v. Charleston*, 11 S. C. 486, 519 (1878); *Seeligson v. Brown*, 61 Texas, 114 (1884); *Pitot v. Johnson*, 33 La. Ann. 1286 (1881); *Smith v. Crescent City, &c., Co.*, 30 La. Ann. 1378 (1878). In regard to stock in national banks, the Federal courts have firmly established the rule that the unregistered transferee is protected against a subsequent attachment or execution. *Continental National Bk. v. Eliot Natl. Bk.*, 5 Fed. Rep. 369 (1881), with a full review of the authorities by Judge Lowell. *Scott v. Pequonnock Natl. Bk.*, 15 Fed. Rep. 494 (1883), where the rule was applied, although the national bank was in Connecticut, a State which strongly favors the opposite rule. The court said: "The tendency of mod-

ern decisions, is to regard certificates of stock attached to an execution blank, assignment, and power to transfer, as approximating to negotiable securities, though neither in form or character negotiable." Even in Massachusetts, where the courts upheld an opposite rule, the State courts will follow the above rule when the stock of a national bank is in question. *Sibley v. Quinsigamond Natl. Bk.*, 133 Mass. 515 (1882), but see *State v. First Natl. Bk. of J.*, 89 Ind. 302 (1883). *Williams v. Mechanics Bk.*, 5 Blatch. 59 (1862), is not in accord with the other Federal decisions. As regards Tennessee, compare *Cornick v. Richards*, 3 Lea, 1 (1879), with *State Ins. Co. v. Sax*, 2 Tenn. Ch. 507 (1875).

¹ *Robinson v. Natl. Bk. of New Berne*, 95 N. Y. 637 (1884). See also *Plymouth Bk. v. Bk. of Norfolk*, 27 Mass. 454 (1830).

chaser at the execution sale, and if the former claims to have purchased the certificate before the attachment or execution was levied, the right of the corporation is clear. It may refuse to allow the registry, and when sued therefor may interplead and compel the claimants to litigate the matter between themselves.¹ But where the corporation does not know whether the outstanding certificate is in the hands of a purchaser or not, and a registry is demanded by a purchaser at an execution sale, the rights and duties of the corporation are not so clear. It has two courses open to it.² It may refuse to allow a registry, until compelled to do so by a court, or it may allow registry without being so compelled. The former is the safer course, since the corporation will probably be thereby protected from all liability to a possible purchaser of the outstanding certificate.³ The corporation, it seems, is protected in its obedience to the decree of a court.⁴ It is quite probable, also, that no court, in any of the above-named States, would require the corporation to issue new certificates of stock to a purchaser of stock at an execution sale, unless such purchaser give to the corporation a bond of indemnity, whereby an unknown purchaser of the outstanding certificate may be protected.⁵ The other course open to the corporation,

¹ See Chap. XXII, § 387. The proper remedy for the purchaser from the judgment-debtor to pursue under such circumstances is to enjoin the corporation and the purchaser at the execution sale from registering the latter as a stockholder. *Smith v. Crescent City, &c., Co.*, 30 La. Ann. 1378 (1878). If an attachment has been levied he should enjoin that. *Cheever v. Meyer*, 52 Vt. 66 (1879).

² *Robinson v. Natl. Bk. of New Berne*, 95 N. Y. 637 (1884).

³ "Where a judicial tribunal of competent jurisdiction of last resort, after a fair contest, in good faith by the corporation, orders the stock to be transferred to the purchaser under such seizure and sale, the corporation cannot be liable to the holder of the certificate who took no steps to protect himself." *Friedlander v. Slaughter House Co.*, 31 La. Ann. 523 (1879). Where, also, the unregistered transferee contested in the courts the right of the purchaser at the execution sale, and was defeated in the lower court, and appealed without staying the decree below, the corporation is not liable for obeying the decree of the lower court, although the appeal is successful. *Chapman v.*

New Orleans Gas Light, &c., Co., 4 La. Ann. 153 (1849).

⁴ See §§ 359, 388.

⁵ The Supreme Court of Ohio, in *Natl. Bk. of N. L. v. Lake Shore & M. S. R. R. Co.*, 21 O. St. 221 (1871), very properly and very distinctly refused to compel a registry, although conceding that the execution purchaser is entitled to dividends. The court said: "Can it be that, because the defendant refused to assume the peril of deciding between the contending claimants, by issuing other certificates for the same stock to the plaintiff upon demand, that it thereby became a wrongdoer and converted the plaintiff's stock to its own use, and rendered itself liable to respond in the full value of the stock to the claimant who could establish his right in a court of law? The very statement of the proposition refutes it." Where the attachment is on stock that the complainant alleges was transferred in fraud of creditors, mandamus will not lie to compel the corporation to allow a registry under the execution sale. *State v. Warren Foundry & M. Co.*, 32 N. J. L. 439 (1868).

that of allowing a registry by the purchaser at the execution sale, without being compelled to do so by a court, is pursued by the corporation at its peril. If it afterwards transpires that the outstanding certificate had been purchased before the attachment or execution was levied, the corporation is liable in damages to such purchaser for allowing the registry,¹ but not unless such purchaser gave a valuable consideration for the certificate, and alleges that fact in his pleading.² Until such purchaser demands a registry from the corporation, it may safely pay dividends to the execution purchaser.³

§ 489. *Rule in Connecticut, Maine, New Hampshire, Vermont, Indiana, Illinois, Wisconsin, and California.*—The courts of these States all hold that where regulations exist, requiring a transfer of stock to be registered on the corporate books in order to be effectual, an attachment or execution levied on stock standing in the defendant debtor's name will cut off the rights of a previous purchaser of the certificate who has not completed his transfer by registry.⁴ Sometimes these regulations requiring a registry are contained in the charter, sometimes only in the by-laws, and sometimes are merely printed on the face of the certificate of stock.⁵ Even in these States, however, it is well established that if the person who levies the attachment or purchases at the execution sale has notice that the defendant debtor had transferred his certificate before the attachment or execution was levied, the purchaser of the outstanding certificate may have

¹ *Smith v. American Coal Co.*, 7 Lans. (N. Y.) 317 (1873). If the purchaser at the execution sale still has the certificates, the purchaser of the old certificate may bring suit against him and the corporation to compel a retransfer. *Rogers v. Stevens*, 8 N. J. Eq. 167 (1849). In a suit by a purchaser at an execution sale to cut off the rights of the judgment-debtor, the corporation is an indispensable party, since it alone can allow a transfer on the books. *St. Louis & San F. Ry. Co. v. Wilson*, 114 U. S. 60 (1884). See also the late case of *Hazard v. Natl. Ex. Bk.*, 26 Fed. Rep. 94 (1886), holding the corporation liable in damages to the purchaser of the outstanding certificate.

² *Littell v. Scranton Gas & Water Co.*, 42 Penn. St. 500 (1862).

³ *Smith v. American Coal Co.*, *supra*.

⁴ See note 5, *sub.*

⁵ *Oxford Turnpike Co. v. Bunnell*, 6 Conn. 552 (1827); *Dutton v. Conn. Bk.*, 13 Conn. 493 (1840), where the provision was in the by-laws; *Skowhegan Bk. v. Cutler*, 49 Me. 315 (1860); *Fiske v. Carr*, 20 Me. 301 (1841); *Pinkerton v. R. R. Co.*, 42 N. H. 424 (1861); *Warren v. Brandon Mfg. Co.*, cited in 52 Vt. 75; *State v. First Natl. Bk. of J.*, 89 Ind. 302 (1883); *Coleman v. Spencer*, 5 Blackf. (Ind.) 197 (1839); *People's Bk. v. Gridley*, 91 Ill. 457 (1879); *Re Murphy*, 51 Wis. 519 (1881), where the provision was by statute. Also under a statute, *Weston v. Bear River, &c., Min. Co.*, 5 Cal. 186 (1855); *Naghe v. Pacific Wharf Co.*, 20 Cal. 529 (1862). If the unregistered purchaser buys the judgment obtained under the attachment, the latter is merged. *Stront v. Natoma Water & Min. Co.*, 9 Cal. 78 (1858).

his remedy. If the attaching creditor has notice before the attachment is levied, the purchaser may obtain a perpetual injunction against the attachment.¹ If, on the other hand, the purchaser at the execution sale has notice, he may be prevented from obtaining registry and claiming the stock.² It is also held that where the unregistered transferee of the certificate of stock has notified the corporation thereof and demanded registry, which is not granted, any attachment or execution levied subsequently to the improper refusal by the corporation to register does not take precedence over such purchaser.³ Where the unregistered purchaser is cut off by an attachment, he cannot compel his vendee to pay for the stock which is made valueless by the attachment.⁴

§ 490. *Rule in Massachusetts.*—The courts of Massachusetts were the first to lay down the rule which places an attachment or execution levy ahead of an unregistered purchaser of the certificate of stock. The evil consequences of the rule however, seem to have become apparent to her courts, and it was held that although the unregistered purchaser was not protected where the charter of the corporation required registry,⁵ yet where only the by-laws or the certificate itself created such a requirement, the unregistered purchaser was protected, and took precedence over

¹ *Cheever v. Meyer*, 52 Vt. 66 (1879); *Scripture v. Francistown Soapstone Co.*, 50 N. H. 571 (1871); *Black v. Zacharie*, 3 How. 482 (1845).

² *People v. Elmore*, 35 Cal. 653 (1868); *Weston v. Bear River, &c.*, Min. Co., 6 Cal. 425 (1856); *Farmers Natl. Gold Bk. v. Wilson*, 58 Cal. 600 (1881), holding also that the execution sale will not be enjoined since the claimant may attend and give notice of his claim. *Newberry v. Detroit, &c., Iron Co.*, 17 Mich. 141, 158 (1868), per Cooley, J. Where the plaintiff bought for itself at the execution sale, and had notice, it is liable *in tort* to the unregistered purchaser of the old certificates. *Bridgewater Iron Co. v. Lissberger*, 116 U. S. 8 (1885). But *Jones v. Latham*, 70 Ala. 164, seems to hold that if the execution is levied without notice of an unrecorded transfer, a subsequent notice before the sale to the purchaser at the sale is ineffectual, and does not affect the latter.

³ *Merchants Natl. Bk. v. Richards*, 6 Mo. App. 454 (1879); *aff'd*, 72 Mo. 77; *Colt v. Ives*, 31 Conn. 25 (1862); *State*

Ins. Co. v. Gennett, 2 Tenn. Ch. 100 (1874); *Plymouth Bk. v. Bk. of Norfolk*, 27 Mass. 454 (1830); *Sargent v. Franklin Ins. Co.*, 25 Mass. 90 (1829). *Contra*, *Fiske v. Carr*, 20 Me. 301 (1841). But not if the transferee merely sends a letter to the corporation requesting a transfer, without sending the evidences of his title and the old certificate. *Newall v. Williston*, 138 Mass. 240 (1885). The corporation is liable in damages if it levies the attachment under such circumstances. *Sargent v. Franklin, &c., Co.*, *supra*. Where registry is allowed, it cuts off a subsequent attachment, even though the transferee has not formally accepted the stock, as required by statute. *Woodruff v. Harris*, 11 U. C. Q. B. 490 (1854).

⁴ *Rock v. Nichols*, 85 Mass. 342 (1862).

⁵ *Fisher v. Essex Bk.*, 71 Mass. 373 (1855); *Newall v. Williston*, 138 Mass. 240 (1885); *Central Natl. Bk. v. Williston*, 138 Mass. 244 (1885); *Boyd v. Rockport Steam Cotton Mills*, 73 Mass. 406 (1856); *Blanchard v. Dedham Gas Light Co.*, 78 Mass. 213 (1858).

the attachment or execution.¹ The legislature of Massachusetts seems to have had a still clearer perception of the demands of trade and of the interests of those who invest in certificates of stock, and, in 1884, enacted a statute which probably will be construed to make an attachment or execution levied on stock no more effective than it is in New York State.²

§ 491. *Shares of stock cannot be subjected to the payment of the stockholder's debts by the process of garnishment.*—The process of garnishment is proper only where a debt is due from a third person to the defendant debtor. It is not a proper remedy for reaching shares of stock owned by the debtor.³ The corporation owes the stockholder no debt, and by no fiction of law can it be held to be a debtor of the defendant debtor. Consequently, where the sheriff levies an attachment, not according to the procedure governing attachments, but according to the procedure of garnishment, the whole proceeding is void, and a subsequent transfer of the stock by the defendant debtor is valid.⁴

¹ *Sargent v. Essex M. Ry. Co.*, 26 Mass. 202 (1829); *Boston Music Hall v. Cory*, 129 Mass. 435 (1880), holding that a delay of four years was not fatal to the unregistered purchaser's rights.

² "The delivery of a stock certificate of a corporation to a *bona fide* purchaser or pledgee for value, together with a written transfer of the same, signed by the owner of the certificate, shall be a sufficient delivery to transfer the title as against all parties; but no such transfer shall affect the right of the corporation to pay any dividend due upon the stock, or to treat the holder of record as the holder in fact, until such transfer is recorded upon the books of the corporation, or a new certificate is issued to the person to whom it has been so transferred." Act

of May 9th, 1884. The enactment of a similar statute is respectfully recommended to the States mentioned in § 489.

³ *Planters & M. Bk. v. Leavens*, 4 Ala. N. S. 753 (1843); *Ross v. Ross*, 25 Ga. 297 (1858), where the court says: "Is stock in this railroad such a debt ('indebtedness') of the railroad to the stockholder that a garnishing creditor of the stockholder can enter up judgment for it against the railroad? It is not; it is a debt which the railroad dares not pay, even to the stockholder himself. The road may pay him *dividends* on it, but that is all." See also *Foster v. Potter*, 37 Mo. 525.

⁴ *Mooar v. Walker*, 46 Iowa, 164 (1877). Cf. *Chesapeake & O. R. R. Co. v. Paine*, 29 Gratt. (Va.) 502.

CHAPTER XXVIII.

AMENDMENTS AND REPEALS OF CHARTERS.

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| <p>§ 492. A corporate charter is a contract between three parties, the State, the corporation, and the stockholders.</p> <p>493. The contract is between the corporation and the stockholders.</p> <p>494. Charter as a contract between the State and the corporation.</p> <p>495. Charter as a contract between the State and the stockholders.</p> <p>496. Stockholders may prevent a repeal of the charter, unless the right is reserved by the State.</p> <p>497. Charter amendments imposed upon the stockholders.</p> | <p>§ 498. Charter amendments offered to the stockholders.</p> <p>499. Auxiliary and incidental amendments are constitutional, though some of the stockholders dissent.</p> <p>500. Material amendments offered to the stockholders can be accepted only by an unanimous vote.</p> <p>501. Amendments under the reserved power of the State to alter, amend, or repeal the charter.</p> <p>502. Dissenting stockholder's remedy against an illegal amendment.</p> <p>503. Assent and acquiescence as a bar to the stockholder's remedy.</p> |
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§ 492. *A corporate charter is a contract between three parties, the State, the corporation, and the stockholders.*—The charter of a corporation having a capital stock, is in reality a contract between three parties, and forms the basis of three distinct contracts.¹ The charter is a contract between the State and the corporation; second, it is a contract between the corporation and the stockholders; third, it is a contract between the stockholders and the State.

§ 493. *The contract is between the corporation and the stockholders.*—That the charter is a contract between the corporation and the stockholders has within the last fifty years been firmly established and is now unquestioned law. The cases of

¹ See *State Bank of Ohio v. Knoop*, 16 How. 369 (1853); *Northern R. R. Co. v. Miller*, 10 Barb. 260 (1851); *Cooley on Constitutional Limitations*, 5th ed., p. 337, where the learned author says: "Those charters of incorporation, however, which are granted, not as a part of the machinery of the government, but for the private benefit or purposes of the corporators, stand upon a different footing, and are held to be con-

tracts between the legislature and the corporators, having for their consideration the liabilities and duties which the corporators assume by accepting them; and the grant of the franchise can no more be resumed by the legislature, or its benefits diminished or impaired without the consent of the grantees, than any other grant of property or valuable thing, unless the right to do so is reserved in the charter itself."

*Natusch v. Irving*¹ in England, and *Livingston v. Lynch*² in this country, followed by a long line of supporting decisions, distinctly hold that the charter is a contract prescribing to the corporation that it shall not attempt to materially change, extend, alter, or abandon the particular business which that charter authorizes the corporation to do. Any attempt of the corporation to make such a change, extension, alteration, or abandonment of that business, is called an *ultra vires* act. It is an act which a single stockholder may prevent by injunction or set aside by a suit in equity. This subject, however, is fully treated in another part of this work.³

§ 494. *Charter as a contract between the State and the corporation.*—As between the State and the corporation, the corporate charter is a contract, protected by that provision of the United States Constitution, which prohibits a State from passing any law which will impair the obligation of a contract.⁴ Hence, it is beyond the power of the State to repeal or materially annul such a corporate charter, unless the power of amendment and repeal has been expressly reserved by the State, or unless all the parties to the contract consent to the change. All the franchises, privileges, and express and implied powers necessary and essential to carrying out the corporate purposes, are protected by this contract.⁵ This branch of the law, however, is not within the scope of this work, except in cases where the corporation neg-

¹ This case, decided by Lord Eldon in 1824, is reported in *Gow on Partnership*, 398.

² 4 Johns. Ch. 573 (1820). Thus in *Clearwater v. Meredith*, 1 Wall. 25, the court says: "The relation between the corporation and the stockholders is one of contract. The stockholder subjects his interest to the control of the proper authorities, to accomplish the object of the organization, but he does not agree that the purpose shall be changed in its character at the will of the directors, or a majority of the stockholders, even. The contract cannot be changed without the consent of both contracting parties."

³ See Ch. XL.

⁴ This rule of law, first enunciated in the case of *Trustees of Dartmouth College v. Woodward*, 4 Wheat. 518 (1819), by Marshall, Ch. J., has become too thoroughly established to be ques-

tioned or to require support by other authorities. In England, the unwritten constitution is not superior to the powers of parliament, and consequently the rule is different. In that country, as is said by Lord Coke, "the power and jurisdiction of parliament is so transcendental and absolute, that it cannot be controlled or confined either for causes or purposes, within any bounds." *Stevens v. Rutland & Burlington R. R. Co.*, 29 Vt. 545 (1854); *Thorpe v. Rutland & Burlington R. R. Co.*, 27 Vt. 140 (1857); *Trustees of Dartmouth College v. Woodward*, 4 Wheat. 518, 643 (1819). Consequently, the English authorities are of little use in this chapter.

⁵ *State Bk. of Ohio v. Knoop*, 16 How. 369 (1853); *Thorpe v. Rutland & Burlington R. R. Co.*, 27 Vt. 140 (1857), per Redfield, J. The latter case discusses the nature of the privilege thus protected.

lects or refuses to protect itself against legislative amendments or repeals, violating the charter contract between the corporation and the State. In such cases, the stockholder may enjoin or remedy the wrong by bringing an action in place of and on behalf of the corporation, making it a party defendant, together with the parties who, under the authority of the State, have violated the contract.¹ A stockholder's action to prevent the payment of a tax levied upon the corporation, in violation of a statutory exemption from taxation, is an action of this character.²

§ 495. *Charter as a contract between the State and the stockholders.*—As between the State and the stockholders also, the corporate charter is a contract protected by the United States Constitution.³ In consequence thereof, the State cannot repeal or materially amend the charter, except by the unanimous consent of the stockholders, unless the power of repeal or amendment is expressly reserved by the State at the time of granting the charter.

§ 496. *Stockholders may prevent a repeal of the charter, unless the right is reserved by the State.*—The repeal by the State of a charter, before the expiration of the time it was to exist, or the repeal at any time, where the charter is perpetual, is an unconstitutional breach of the contract between the State and the corporation and the stockholders.⁴ Where, however, the right of

¹ *Greenwood v. Freight Co.*, 105 U. S. 13 (1881). The character of such an action, also the parties, pleadings, and rules of relief, are explained in Part IV.

² *Dodge v. Woolsey*, 18 How. 331 (1855); *State Bk. of Ohio v. Knoop*, 16 How. 369 (1853). See also *Wilmington R. R. v. Reid*, 13 Wall. 264 (1871); *Delaware R. R. Tax*, 18 Wall. 206 (1873). See Chapter on Taxation.

³ "A charter of incorporation granted by a State creates a contract between the State and the corporators, which the State cannot violate." This has been held so often by this court that "it is supererogation to repeat it." *Wilmington R. R. v. Reid*, 13 Wall. 264 (1871). It "has been the settled law of this court since the Dartmouth College case." *Delaware R. R. Tax*, 18 Wall. 206 (1873).

To the same effect see *Zabriskie v. Hackensack & N. Y. R. R. Co.*, 18 N. J. Eq. 178 (1867); *Lothrop v. Stedman*, 42 Conn. 583 (1875); *Stevens v. Rutland & Burlington R. R. Co.*, 29 Vt. 545 (1854). "An act granting corporate privileges to a body of men is, when accepted, a contract between the State and the corporators. . . . It is sustained by everything that we are bound to regard as authority," by the courts, by the opinion of the legal profession, and by the acquiescence of the people. *Erie & North-east. R. R. v. Casey*, 26 Pa. St. 287 (1856), per Jeremiah Black, J.

⁴ *Greenwood v. Freight Co.*, 105 U. S. 13 (1881). "A grant of corporate privileges for a specified period cannot be resumed by the State within such period. If the charter be without limitation as to time, it is forever irrepealable." *Erie*

repeal is reserved by the legislature, then such reservation becomes a part of the contract, and the repeal of the charter rests in the discretion of the legislature.¹ Upon a repeal, the corporate property becomes a trust fund, to be applied first to the payment of the debts of the corporation, and the balance to be distributed among the stockholders.²

§ 497. *Charter amendments imposed upon the stockholders.*—

The right of the legislature to amend a charter against the will of the stockholders has been the subject of much litigation. Such amendments are clearly divisible into two kinds. The first are those which, by their terms, are absolute and compulsory, and do not depend for their existence upon the action or willingness of the corporation or the stockholders to accept them.³ Of such

& Northeast. R. R. v. Casey, *ubi supra*. The legislature cannot repeal, nor can it forfeit a charter. Forfeiture can be decreed only by the courts. It is not a legislative function. Allen v. Buchanan, 9 Phil. (Pa.) 283 (1873).

¹ Under a reserved power to repeal at the pleasure of the legislature, the courts cannot question the necessity nor the legislative motives leading to a repeal. Greenwood v. Freight Co., 105 U. S. 13 (1881); Lothrop v. Stedman, 13 Blatchf. 134 (1875). See Sinking Fund Cases, 99 U. S. 700, 720 (1878); Northern R. R. Co. v. Miller, 10 Barb. 260 (1851). If the power of repeal arises only upon an abuse of franchise, the court may review the question whether there was an abuse. Erie & Northeast. R. R. v. Casey, *supra*; Mayor, &c. of Baltimore v. Pittsburgh & Connellsville R. R. Co., 1 Abb. U. S. Rep. 9 (1865); Flint, &c. Plank Road Co. v. Woodhull, 25 Mich. 99. Under this reserved power, the State may authorize one corporation to build its road on a route which a prior corporation has designated, but not acquired. *Re Cable Ry.*, Supreme Ct., N. Y. Daily Reg., March 27th, 1886. A general statute or constitutional provision reserving the right to repeal, alter, or amend charters, enters into all charters granted subsequent thereto as much as if actually inserted in such charters. *Re Lee's Bk. of Buffalo*, 21 N. Y. 9 (1860); Commissioners, &c. v. Holyoke Water Power Co., 104 Mass. 446 (1870).

² Lothrop v. Stedman, 13 Blatchf. 134 (1875); McLaren v. Pennington, 1 Paige,

102 (1828), by statute; Detroit v. Detroit & Howell Plank Road Co., 43 Mich. 140 (1880); County of San Mateo v. Southern Pacific R. R. Co., 8 Sawyer, 238, per Field, J., holding that "the property of the corporation acquired in the exercise of its functions is held independently of such reserved power, and the State can only exercise over it the control which it exercises over the property of individuals engaged in similar business," p. 279. The reserved power may affect the franchises, but not the property of the corporation. A repeal of the franchise of a railroad company vests in the people of the State, not only the franchise to be a corporation, but also the franchise of the right of way acquired by the railroad company by legislative grant or under the powers of eminent domain delegated to it by the State. The road-bed of the railroad upon repeal of the charter reverts to the State and belongs to it. Erie & North East R. R. v. Casey, *supra*. Cf. New York, &c., R. R. Co. v. Parmelee, 1 Ohio C. C. Rep. 239, holding that the right of way reverts in the owner of the fee. This question is involved in the litigation, now pending, growing out of the repeal of the charter of the Broadway Street Railway Company of New York city.

³ Such amendments are unconstitutional and void, unless made under a reserved power to amend. The case of Cross v. Peach Bottom Ry. Co., 90 Pa. St. 392 (1879), holds that "The legislative reservation is in the nature of a police power, designed for the protection of the public welfare, and where such protection

a kind are amendments increasing the liability of stockholders on their stock. A statute passed subsequent to the granting of a charter and increasing the liability of a stockholder on his stock, is unconstitutional and void, unless the legislature has reserved the right to alter or amend the charter.¹ Under such a reservation the statute is legal and binding.²

becomes necessary, the law-making power may act without consulting either the interests or will of the company and in such case it may well be that not only the company but its stockholders must submit. . . . The reservation . . . was only intended to enable the legislature to act without the consent and against the will of the corporation." Where the amendment is for the benefit and at the suggestion of the corporation, different rules are held to apply.

¹ Thus in a case of a statute authorizing the taxation of stock which by the corporate charter is exempt, the statute is unconstitutional. *Gordon v. Appeal Tax Court*, 3 How. 133 (1845); *Farrington v. Tennessee*, 95 U. S. 679 (1877). See Chapter on Taxation.

² It certainly is as regards corporate debts already incurred. *Commonwealth v. Cochituate Bk.*, 8 Mass. 42; *Wheeler v. Frontier Bk.*, 23 Me. 308. And has been held to be so as regards future corporate debts. *Ireland v. Palestine, &c., Turnpike Co.*, 19 O. St. 369 (1869). *Contra, Stanley v. Stanley*, 26 Me. 191 (1846); *Coffin v. Rich*, 45 Me. 507 (1858). A statute imposing additional liability upon the shareholders cannot be repealed so as to affect those who were corporate creditors previously to the repeal. *Hawthorne v. Calef*, 2 Wall. 10 (1864); *Conant v. Van Shaick*, 24 Barb. 87 (1857); *Norris v. Wrenschall*, 34 Md. 492 (1871); *Provident Savings Institution v. Jackson Place, &c., Co.*, 52 Mo. 552 (1873); *St. Louis R. R., &c. Co. v. Harbine*, 2 Mo. App. 134; *Central, &c. Mechanical Association v. Alabama, &c. Insurance Co.*, 70 Ala. 120; *Woodruff v. Trapnall*, 10 How. 190. See also *Story v. Furman*, 25 N. Y. 214 (1862); *Rochester v. Barnes*, 26 Barb. 657 (1858); *Sinking Fund Cases*, 99 U. S. 700 (1878). *Cf. Jerman's Admr. v. Benton*, 79 Mo. 148; *Woodhouse v. Commonwealth Ins. Co.*, 54 Pa. St. 307 (1867). And it is said that a stockholder may restrain by a proper proceeding the acceptance by the corporation of an unconditional amendment to the charter by which

the liability of the shareholders is increased. *Owen v. Purdy*, 12 Ohio St. 73 (1861); *Fry's Exec. v. Lexington, &c. R. R. Co.*, 2 Metc. (Ky.), 314. *Cf. Bailey v. Hollister*, 26 N. Y. 112 (1862); *Thompson v. Guion*, 5 Jones' Eq. (N. C.) 113; *Mowrey v. Indianapolis, &c. R. R. Co.*, 4 Biss. 78; *Lauman v. Lebanon Valley R. R. Co.*, 30 Penn. St. 42; *Hamilton, &c. Insurance Co. v. Hobart*, 2 Gray, 543; *Gardner v. Hamilton, &c. Insurance Co.*, 33 N. Y. 421 (1865). Frequently, and now almost universally, the legislature has a reserved power to alter, amend, or repeal the charters of corporations granted by it. *New York const.* of 1846, art. 8, §§ 1 & 2; *Matter of New York Elevated R. R. Co.*, 70 N. Y. 327 (1877); *Johnson v. Hudson River R. R. Co.*, 49 Id. 455 (1872); *Bank of Chenango v. Brown*, 26 Id. 467 (1863); *Ashuelot R. R. Co. v. Elliot*, 58 N. H. 451, 454; *Taylor on Corporations*, § 496 *et seq.* Under this reserved power the legislature, it is held, may impose a statutory liability, in addition to the liability at common law, upon stockholders after they have been incorporated and gone into business under a charter which does not impose such liability. The exercise of this power by the legislature, in such a case, is held to be only a repeal of part of the corporate franchises. *South Bay Meadow Dam Co. v. Gray*, 30 Me. 547 (1849). *Cf. Close v. Glenwood Cemetery*, 107 U. S. 466 (1882). So also it is said that under this reserved power the legislature may impose a statutory liability for the future debts and obligations of the corporation. *Sherman v. Smith*, 1 Black, 587 (1861); *Matter of Lee's Bank of Buffalo*, 21 N. Y. 9 (1860); *Matter of the Empire City Bank*, 18 Id. 199 (1858). *Cf. Bailey v. Hollister*, 26 N. Y. 112 (1862); *Sinking Fund Cases*, 99 U. S. 700 (1878); *Oldtown, &c. R. R. Co. v. Veazie*, 39 Me. 571; *Green v. Biddle*, 8 Wheaton, 1, 84; *Gardner v. Hope Ins. Co.*, 9 R. I. 194 (1869). Such increased liability may be imposed by a new constitution of the State. *Re Reciprocity Bk.* 22 N. Y. 9 (1860); *Re Empire Bk.*, 18

§ 498. *Charter amendments offered to the stockholders.*—The second class of amendments to a charter, the amendments which occur most frequently and give rise to many difficulties, are those which allow the corporate directors or a majority of the stockholders in corporate meeting assembled to engage in a new or different or more extensive or more contracted business than that authorized by the original and unamended charter.

§ 499. *Auxiliary and incidental amendments are constitutional, though some of the stockholders dissent.*—An amendment made to a corporate charter is either a material and fundamental change from the original plan, or it is an auxiliary and incidental change, consistent with the carrying out of the original plan.¹ The latter class of amendments are constitutional and valid. The acceptance of auxiliary amendments may be within the power of the directors or it may rest with a majority of the stockholders.² An amendment may be said to be auxiliary and incidental when it merely grants new powers or authorizes new methods and new plans for the purpose of carrying out the original plan and effecting the real object of that plan.³ Whether an

N. Y. 199 (1858); *Re Lee's Bk. of Buffalo*, 21 N. Y. 9 (1860); *aff'd, sub nom. Sherman v. Smith*, 1 Black, 587 (1861). In *The Consolidated Assoc'n v. Lord*, 35 La. Ann. 425 (1883), where the court refused to uphold an amendment which imposed further liability on the stockholder, the court said: "The horde of officers—president, vice-president, cashier, receivers, directors—pass before us in this record in lengthened procession, laden with salaries and plethoric with stipends, and the lean and slippered stockholder, gaunt from forty years exhaustion, at last holds up his hands in eager, passionate supplianee for relief from this insatiate, ever-recurring hunger for more contributions."

Whenever the statute imposing the liability is penal in its nature, a repeal of it, even so as to affect existing debts, is not unconstitutional. *Breitung v. Lindauer*, 37 Mich. 217; *Union Iron Co. v. Pierce*, 4 Biss. 327; *Gregory v. German Bank*, 3 Col. 382.

¹ The general principle of law governing this branch of the subject is well expressed in *Woodfork v. Union Bk.*, 3 Coldw. (Tenn.) 488 (1866). "The contract, or charter, after acceptance, is inviolable between the State and the corporation, as it is also between the corporation

and stockholders. Neither the one nor the other can disregard its obligations, or alter its essential franchises, without the unanimous concurrence of the stockholders. . . . If the alterations proposed in the charter of a private corporation by legislative enactment are merely auxiliary and not fundamental, they may be accepted by a majority of the corporators; and when, so assented to, they are binding on the whole, but it is otherwise . . . when the alterations are fundamental, radical, and vital. The acceptance must then be unanimous."

² *Ill. River R. R. Co. v. Zimmer*, 20 Ill. 65 (1858). Ordinarily the acceptance cannot be by the directors. *Marlborough Mfg. Co. v. Smith*, 2 Conn. 579; *Brown v. Fairmount Mine Co.*, 10 Phil. 32. *Cf. Blatchford v. Ross*, 5 Abb. Pr. (N. S.) 434. *Contra, Venner v. Atchison, &c.*, R. R. Co., 28 Fed. Rep. 581 (1886). Where the amendment is not fundamental it may be accepted by a majority. *Buffalo & N. Y. City R. R. Co. v. Dudley*, 14 N. Y. 336 (1856); *Schenectady & Saratoga Plank Road Co. v. Thatcher*, 11 N. Y. 102 (1854); *Dayton, &c., R. R. Co. v. Hatch*, 1 Disney, 84 (1855); *Com'th v. Cullum*, 13 Penn. St. 133. And see *sub.*

³ The individual motives and interests

amendment materially changes the corporate plans or not is a question of law for the court upon facts ascertained by the jury.¹ Accordingly each case is to be decided according to the peculiar circumstances of that case, and no general rules can be laid down which will apply to all cases.²

of a stockholder are disregarded. Whatever is for the benefit of the corporation is conclusively presumed to be for the benefit of each stockholder. A change immaterial to the corporation is immaterial to each and every stockholder. *Supervisors of Fulton County v. Miss. & Wabash R. R. Co.*, 21 Ill. 338 (1859); *Delaware R. R. Co. v. Tharp*, 1 Hous. (Del.) 149 (1856); *Irvine v. Turnpike Co.*, 2 Penn. & W. 466; *Ill. Riv. R. R. Co. v. Zimmer*, 20 Ill. 654 (1858); *Sprague v. Ill. River R. R. Co.*, 19 Ill. 174; *Banet v. Alton & Sangamon R. R. Co.*, 13 Ill. 504 (1851). *Cf. Hester v. Memphis & Charleston R. R. Co.*, 32 Miss. 378 (1856); *Witter v. Miss., Ouachita & Red River R. R. Co.*, 20 Ark. 463 (1859); *The cases of Zabriskie v. Hackensack & N. Y. R. R. Co.*, 18 N. J. Eq. 178 (1867); *Dayton & Cincinnati R. R. Co. v. Hatch*, 1 Disney, 84; and *Central R. R. Co. v. Collins*, 40 Ga. 617, repudiate the distinction between the material and immaterial changes. All changes are held to be equally material.

¹ *Winter v. Muscogee R. R. Co.*, 11 Ga. 438 (1852); *Witter v. Miss., Ouachita & Red River R. R. Co.*, 20 Ark. 463 (1859); *Memphis Branch R. R. Co. v. Sullivan*, 57 Ga. 240 (1876). *Cf. Southern Penn. Iron & R. R. Co. v. Stevens Ex'r*, 87 Pa. St. 190 (1878).

² Certain changes in the route of a railroad have been held to be immaterial, *Willson v. Willes Valley R. R. Co.*, 33 Ga. 466 (1863); *Johnson v. Pensacola & Ga. R. R. Co.*, 9 Fla. 299 (1860); *Peoria & Oquawka R. R. Co. v. Elting*, 17 Ill. 429 (1856); *Banet v. Alton & Sangamon R. R. Co.*, 13 Ill. 504 (1851); building branch lines, *Peoria & Rock Island R. R. Co. v. Preston*, 35 Iowa, 115 (1872); *Greeneville & Columbia R. R. Co. v. Coleman*, 5 Rich. Law (S. C.), 118 (1851); *Peoria & Oquawka R. R. Co. v. Elting*, 17 Ill. 429 (1856); issuing preferred stock, *Everhart v. West Chester & Phila. R. R. Co.*, 28 Pa. St. 339 (1857); *Rutland & Burlington R. R. Co. v. Thrall*, 35 Vt. 536 (1863); or more common stock, *City of Cov. v. Cov. & Cin. Bridge Co.*, 10 Bush, 69 (1873); extending the time for

completing the road, *Agri. Branch R. R. Co. v. Winchester*, 13 Allen, 29 (1866); *Poughkeepsie, &c. Co. v. Griffin*, 24 N. Y. 150 (1861); *Bailey v. Hollister*, 26 N. Y. 112 (1862); power to amend being reserved, *Taggart v. Western R. R. Co.*, 24 Md. 563 (1866); *Danbury, &c. R. R. Co. v. Wilson*, 22 Conn. 435 (1853); consolidations that take the place of part of the line as laid out, *Sprague v. Ill. River R. R. Co.*, 19 Ill. 174 (1857); *Hanna v. Cin. & Fort Wayne R. R. Co.*, 20 Ind. 30 (1863); change of corporate name, *Bucksport & Bangor R. R. Co. v. Buck*, 68 Me. 81 (1878); *Clark v. Monongahela Nav. Co.*, 10 Watts (Tenn.), 364 (1840); changing the terminus, *Pacific R. R. v. Renshaw*, 18 Mo. 210 (1852); *Ross v. Chicago, &c. R. R. Co.*, 77 Ill. 134; reduction of capital stock and shortening of the road, *Troy & Rutland R. R. Co. v. Kerr*, 17 Barb. 581 (1854); or enlarging the capital stock and extending the road, such changes not appearing on the record to be detrimental, *Peoria & Oquawka R. R. Co. v. Elting*, 17 Ill. 429 (1856); *Rice v. Rock Island R. R. Co.*, 21 Ill. 93; and minor changes in general, *Union Agri. & Stock Ass'n v. Mill*, 31 Iowa, 95 (1870); also extensive changes, *Ill. River R. R. Co. v. Zimmer*, 20 Ill. 654 (1858); such as extending the road, *Cross v. Peach Bottom Ry. Co.*, 90 Pa. St. 392 (1879); purchasing another railroad, *Venner v. Atchison, &c. R. R. Co.*, 28 Fed. Rep. 581 (1886); or increasing the number of directors, *Mower v. Staples*, 32 Minn. 284 (1884). See also *Gray v. Coffin*, 9 Cush. 192 (1852); *Child v. Coffin*, 17 Mass. 64 (1820); *Langley v. Little*, 26 Me. 162 (1846); *Covington v. Bridge Co.*, 10 Bush, 69, 78 (1873); *Payson v. Withers*, 5 Biss. 269 (1873); *Joy v. Jackson, &c. Co.*, 11 Mich. 155 (1863). See also *Fry's Ex'rs v. Lexington, &c. R. R. Co.*, 2 Metc. (Ky.) 322; *Waring v. Mayor, &c. of Mobile*, 24 Ala. 201; *Bank v. Richardson*, 1 Me. 79; *Greenville, &c. R. R. Co. v. Johnson*, 8 Baxt. 332; *State v. Accommodation Bk. of La.*, 26 La. Ann. 288; *Fall River Iron Works v. Old Colony R. R. Co.*, 5 Allen, 221; *Pacific, &c. R. R. Co. v. Hughes*, 22 Mo. 297.

§ 500. *Material amendments offered to the stockholders can be accepted only by an unanimous vote.*—On the other hand a material and fundamental change in the charter by an amendment to that charter is an unconstitutional violation of the contract rights of any stockholder who does not assent to such an amendment. Considerable difficulty is experienced in determining what is a material and fundamental change. Each case is decided upon its own facts, and consequently the best light as to the spirit of what constitutes a material change is obtained by a study of the facts of cases which have been decided.¹

¹ Under the circumstances of the cases, it has been held a material change to shorten and vary the route, *Winter v. Muscogee R. R. Co.*, 11 Ga. 438 (1852); to vary the route, *Middlesex Turnpike Corporation v. Locke*, 8 Mass. 268 (1811); *Id. v. Swan*, 10 Mass. 384 (1813); *Hester v. Memphis & Charleston R. R. Co.*, 32 Miss. 378 (1856); *Witter v. Miss.*, *Ouachita & Red River R. R. Co.*, 20 Ark. 463 (1858); *Champion v. Memphis, &c., R. R. Co.*, 35 Miss. 692; *Simpson v. Denison*, 10 Hare, 54; changing a terminus, *Manheim, &c., Co. v. Arndt*, 31 Penn. St. 317 (1858); *Marietta, &c., R. R. Co. v. Elliott*, 10 O. St. 57; *Middlesex, &c., Co. v. Locke*, 8 Mass. 267; *Id. v. Swan*, *Id.* 385; *Thompson v. Guion*, 5 Jones' Eq. 113; permitting a railroad to go into water transportation business, *Hartford & New Haven R. R. Co. v. Croswell*, 5 Hill, 383 (1843), a leading case; *Marietta & Cin. R. R. Co. v. Elliott*, 10 O. St. 57 (1859); shortening the line, *Bk. v. City of Charlotte*, 85 N. C. 433 (1881); allowing business to be commenced before the full capital stock is subscribed, *Memphis Branch R. R. Co. v. Sullivan*, 57 Ga. 240 (1876); dividing the line, and forming two or more corporations, *Leed & Evensburg Turnpike Road Co. v. Phillips*, 2 Penr. & Watts (Pa.), 184; *Supervisors of Fulton County v. Miss. & Wabash R. R. Co.*, 21 Ill. 338 (1859); *Carlisle v. Terre Haute & Richmond R. R. Co.*, 6 Ind. 316 (1855); making the charter perpetual, and increasing power to hold property, *Prop. of the Union Lock & Canals v. Towne*, 1 N. H. 44 (1817); allowing a life insurance company to insure against fire and marine loss, *Ashton v. Burbank*, 2 Dill. 435; extending the line, *Stevens v. Rutland & Burlington R. R. Co.*, 29 Vt. 545 (1855). See also *Noesen v. Town of Port Washington*,

37 Wis. 168 (1875), where there was no amendment authorizing the purchase of a railroad running at right angles to the old, but a release was upheld; increasing the par value of the stock, *Mahon v. Wood*, 44 Cal. 462 (1872); consolidating the corporation with another corporation, *Ill. Grand Trunk R. R. Co. v. Cook*, 29 Ill. 237 (1862); *McCray v. Junction R. R. Co.*, 9 Ind. 358 (1857); *Shelbyville & Rushville Turnpike Co. v. Barnes*, 42 Ind. 498 (1873); *Booe v. Junction R. R. Co.*, 10 Ind. 93 (1857); *New Orleans, Jackson, & Great Northern R. R. Co. v. Harris*, 27 Miss. 517 (1854); *Clearwater v. Meredith*, 1 Wall. 25 (1863); *Kean v. Johnson*, 1 Stock. (9 N. J. Eq.) 401 (1853); *Black v. Del. & Raritan Canal Co.*, 24 N. J. Eq. 455 (1873); criticised in *Mowrey v. Ind. & Cin. R. R. Co.*, 4 Biss. 78. *Cf. Lanman v. Lebanon Valley R. R. Co.*, 30 Pa. St. 42 (1858); *Fry's Executor v. Lexington, &c., R. R. Co.*, 2 Metc. (Ky.) 314 (1859), the court saying: "Each shareholder in an incorporate company has a right to insist on the prosecution of the particular objects of the charter. He cannot be deprived of his rights or privileges without his assent. Such alterations of the charter as are necessary to carry into effect its main design may be made without his consent. But an alteration which materially and fundamentally changes the responsibilities and duties of the company, or which superadds an entirely new enterprise to that which was originally contemplated, may be resisted by the stockholders, unless such alterations are provided for in the charter itself, or in the general laws of the State in force at the time the act of incorporation was passed." Until, however, the corporation accepts such amendment, the stockholders cannot complain. To same effect, *Delaware, &c., R. R. Co. v. Irick*, 23 N. J. L. 321 (1852). See in

§ 501. *Amendments under the reserved power of the State to alter, amend, or repeal the charter.*—The extent of the power of the legislature to amend a charter, where it has reserved that power, is not yet fully settled, and is full of difficulties. There is a strong tendency in the decisions, and a tendency which is deserving of the highest commendation, to limit the power of the legislature to amend a charter under this reserved power. It should be restricted to those amendments only in which the State has a public interest. Any attempt to use this power of amendment for the purpose of authorizing a majority of

general, *Pearce v. Madison R. R. Co.*, 21 How. 441; *Tuttle v. Mich. Air Line Co.*, 35 Mich. 247; *New Jersey, &c., R. R. Co. v. Strait*, 35 N. J. L. 322; *Sprague v. Ill. R. R. Co.*, 19 Ill. 174; *Comth. v. Culom*, 13 Penn. St. 133 (1850). In all these cases neither a mandatory statute, nor a vote of the directors, nor a majority of the stockholders, can compel a dissenting stockholder to accept the change. It would be unconstitutional. The stockholder may say: "I have agreed to become interested in a railroad company, and have contracted in view of the profits to be expected and the perils and losses incident to that description of business; but I have not agreed that those to be intrusted with the capital I contribute shall have power to use it in a business of a different character, and attended with hazards of a different description." *Marietta, &c., R. R. Co. v. Elliott*, 10 O. St. 57 (1859). The legislature cannot, in the amendment itself, authorize the majority to bind the minority herein. *New Orleans, &c., R. R. Co. v. Harris*, 27 Miss. 517. On the right of a dissenting stockholder in general, see also *Goodin v. Evans*, 18 O. St. 150, 166 (1868); *Railway Co. v. Allerton*, 18 Wall. 233, 235; *Printing House v. Trustees*, 104 U. S. 711; *Brown v. Fairmount Min. Co.*, 10 Phila. 32; *Roberts' Appeal*, 92 Penn. St. 407; *Buffalo, &c., R. R. Co. v. Potter*, 18 Barb. 21; *Hoey v. Henderson*, 32 La. Ann. 1069; *Waring v. Mayor, &c., of Mobile*, 24 Ala. 701; *Old Town, &c., R. R. Co. v. Veazie*, 39 Me. 571; *Miss., &c. R. R. Co. v. Cross*, 20 Ark. 443; *Clinch v. Financial Co.*, L. R. 4 Ch. 117; *Dougan's Case*, L. R. 8 Ch. 540; *Barrett v. Alton, &c., R. R. Co.*, 13 Ill. 504; *Peoria, &c., R. R. Co. v. Elting*, 17 Ill. 429; *Ill., &c., R. R. Co. v. Zimmer*, 20 Id. 654; *Rice v. Rock Island R. R. Co.*, 21 Id. 93; *Ross v. C. B. & Q. R. R.*

Co., 77 Id. 134; *Pacific, &c., R. R. Co. v. Renshaw*, 18 Mo. 210; *Id. v. Hughes*, 22 Id. 297. See also *Gray v. Monongahela Nav. Co.*, 2 Watts & S. 156; *Delaware R. R. Co. v. Tharp*, 1 Houst. 174; *Martin v. Pensacola R. R. Co.*, 8 Fla. 381; *Dayton, &c., R. R. Co. v. Hatch*, 1 Disney, 84; *Currie v. Mut. Ass. Soc.*, 4 Hen. & M. 315; *Covington v. Covington, &c., R. R. Co.*, 10 Bush, 69; *Zabriskie v. Cleveland, &c., R. R. Co.*, 23 How. 381; *Cincinnati, &c., R. R. Co. v. Cole*, 29 O. St. 126; *St. Mary's Church, 7 Serg. & R. 517*; *Vermont, &c., R. R. Co. v. Vermont, &c., R. R. Co.*, 34 Vt. 2, 50, 51; *Owen v. Purdy*, 12 O. St. 73; *Lyons v. Orange, &c., R. R. Co.*, 18 Md. 32; *Ill. Riv. R. R. Co. v. Beers*, 27 Ill. 185; *Hope Ins. Co. v. Beckman*, 47 Mo. 93; *Id. v. Koeller*, 47 Id. 129; *Wetumpka & Coosa R. R. Co. v. Bingham*, 5 Ala. 657; *Palfrey v. Paulding*, 7 La. Ann. 363; *State v. Sibley*, 25 Minn. 387; *Bangor, &c., R. R. Co. v. Smith*, 47 Me. 34; *Sheilds v. Ohio*, 26 O. St. 86; *s. c.*, 95 U. S. 319; *State v. Maine, &c., R. R. Co.*, 66 Me. 488; *s. c.*, 96 U. S. 499; *New Jersey v. Yard*, 95 Id. 113; *s. c.*, *contra*, 37 N. J. L. 228; *Smead v. Indianapolis, &c., R. R. Co.*, 11 Ind. 104; *Sumrall v. Mut. Ins. Co.*, 40 Mo. 27; *Kenton Co. Court v. Bank Lick Turnp. Co.*, 10 Bush, 525; *Regents v. Williams*, 9 Gill & J. 365; *s. c.*, 31 Am. Dec. 72; *St. John's College v. Purnell, &c.*, 23 Md. 629; *White v. Syracuse R. R. Co.*, 14 Barb. 560; *Schenectady, &c., Plank R. Co. v. Thatcher*, 11 N. Y. 102; *Caley v. Philadelphia, &c., R. R. Co.*, 60 Penn. St. 363 (1876). See also *Burlington, &c., R. R. Co. v. White*, 5 Iowa, 409 (1857); *South Georgia, &c., R. R. Co. v. Ayres*, 56 Ga. 230 (1876), where, however, a sale of the road was made without legislative authority.

the stockholders to force upon the minority a material change in the enterprise, is contrary to law and the spirit of justice. Under such reserved power the legislature has the same rights to amend the charter that it would have had in case the Dartmouth College case had decided that charters were not contracts.¹ The power to make amendments and to repeal and alter charters has been reserved in most of the States of the Union.² It is clearly established that the legislature cannot, under this reserved power, amend the charter so as to change the whole character of the enterprise and compel the corporation to proceed under the amended charter.³ An amendment under the reserved power cannot change the character of the enterprise, nor take away rights already acquired under the charter. It must not be foreign to the purposes and objects of the original charter.⁴

¹ *County of San Mateo v. Southern Pacific R. R. Co.* 8 Sawyer, 238, 279 (1882); *Detroit v. Detroit & Howell Plank Road Co.*, 43 Mich. 140 (1880).

² Constitution of Ala. XIII, 1; Ark. V, 48; Cal. IV, 31; 1879, XII, 1; Col., 1876, XV, 3; Del. II, 17; Iowa, VIII, 12; Kan. XII, 1; Me. Laws of 1831; Mass. St. 1830, ch. 81, R.'S. ch. 44, § 23, Gen. St. ch. 68, § 41; Md. III, 48, par. 2; Mich. XV, 1, 8; Mo. VIII, 14; N. J. Amend. IV, 7, par. 11, cl. 11; N. Y. VIII, 1, R. S. pt. I, ch. XVIII, Title 3, § 8; N. Car. VIII, 1; Neb., 1875, XI; Nev. VIII, 1; O. XVIII, 2; Or. XI, 2; Penn. XVI, 10; S. Car. XII, 1; Tenn. XI, 8; Tex., 1875, XII, 5, 7; Wis. XI, 1.

³ In Pennsylvania it is held that the reserved power, when used so as to make an amendment compulsory on the corporation, "is in the nature of a police power, designed for the protection of the public welfare." *Cross v. Peach Bottom Ry. Co.*, 90 Pa. St. 392 (1879). "The power of amendment was never reserved with reference to any question between the corporation and its stock subscribers, but solely with reference to questions between the corporation and the State, where the latter desired to make compulsory amendments against the will of the former." The corporation cannot be compelled to proceed. All the State "can do is to grant it the power, and then it is for the corporation to accept it or not, as it pleases." *Kenosha, Rockford & Rock Island R. R. Co. v. Marsh*, 17 Wis. 13 (1862); *Troy & Rutland R. R. Co. v. Kerr*, 17 Barb. 581 (1854). In the *City*

of *Knoxville v. Railroad Co.*, 22 Fed. Rep. 758 (1884), the court says: "It was not competent for the legislature to do more in this respect than to waive the public rights. It could not divest or impair the rights of the shareholders, as between themselves, as guaranteed by the company's charter, without their consent. It was upon the faith of the stipulations contained in said charter that the shareholders subscribed to the capital stock, and thereby made themselves members of the corporation." In the case also of *Orr v. Bracken County, &c.*, 81 Ky. 593 (1884), an amendment under the reserved power, changing the method of voting, was decided to be of no effect until the stockholders accepted it. The court said: "The right to amend the charter may be expressly reserved, but that right does not confer the favor of taking from the corporators the control of the corporate property." Query, whether a mandatory consolidation would be legal. *Mowrey v. Ind. & Cin. R. R. Co.*, 4 Biss. 78 (1866). When legal, a mandatory change does not require acceptance by the stockholders. *Zabriskie v. Hackensack & N. Y. R. R. Co.*, 18 N. J. Eq. 178 (1867). But when the mandatory amendment goes beyond the legal limits, it must be accepted by the corporation as though it were made optional with the corporation. *Kenosha, Rockford & Rock Island R. R. Co. v. Marsh*, 17 Wis. 13 (1863).

⁴ This power has its limits. "It can repeal or suspend the charter, it can alter or modify it, it can take away the charter, but it cannot impose a new one and

It may, however, go to any extent in authorizing the corporation itself, by an unanimous vote of the stockholders, to make fundamental changes. The latest and best view taken of this reserved power of the State, is that under it a fundamental amendment to the charter does not authorize a majority of the stockholders to accept the amendment and proceed, but that unanimous consent of the stockholders is necessary.¹

oblige the stockholders to accept it. . .

. . . The power to alter and modify does not give power to make any substantial additions to the work." *Zabriskie v. Hackensack & N. Y. R. R. Co.*, 18 N. J. Eq. 178 (1867). "The power of alteration and amendment is not without limit; the alterations must be reasonable; they must be made in good faith, and be consistent with the scope and object of the act of incorporation. Sheer oppression and wrong cannot be inflicted under the guise of amendment or alteration." *Shields v. Ohio*, 95 U. S. 325 (1877); *Spring Valley Water Works v. Bd. of Supervisors of San Francisco*, 61 Cal. 3 (1881). The amendment must "not defeat or subsequently impair the object of the grant, or any rights vested under it." *Close v. Glenwood Cemetery*, 107 U. S. 466 (1882). See also *Miller v. State*, 15 Wall. 478 (1872); *Mayor, &c., of Worcester v. Norwich & Worcester R. R. Co.*, 109 Mass. 103 (1871). The motives of the legislators cannot be inquired into. *Northern R. R. Co. v. Miller*, 10 Barb. 260 (1851); *Matter of Elevated R. R. Co.*, 70 N. Y. 327, 351 (1877).

¹ *Mills v. Central R. R. Co.*, 41 N. J. Eq. 5 (1886), where a statute subsequent to the charter, authorized the consolidation of railroad companies. The court said: "The provision in that act, that it shall be lawful to lease or consolidate, is merely a legislative authorization, a concession on the part of the legislature, of the power to do that which could not lawfully be done without such authority. It is not an enactment, that the directors may, without the consent of the stockholders of the company, lease, consolidate, or merge. Nor is it in effect an enactment, that they may with the consent of the majority of the stockholders do so. But the statute is merely an enabling act, a law intended to give, once for all, a general legislative authority to lease, consolidate, or merge. The legislature did not intend to affect the rights of stock-

holders, *inter sese*, and the act does not do so, either expressly or by implication.

. . . After shareholders had entered into a contract among themselves, under legislative sanction, and expended their money in the execution of the plan mutually agreed upon, the plan could not, even by virtue of legislative enactment, be radically changed by the majority alone, and dissentient stockholders be compelled to engage in a new and totally different undertaking, because such action would impair the obligation of the dissenting stockholders' contract with their associates and the State." The court said also, that under its reserved power to amend a charter, the State cannot give "a power to one part of the corporators as against the other, which they did not have before." It has been held, however, that under its reserved power, the legislature may authorize a road to lease another. *Durfee v. Old Colony & Fall River R. R. Co.*, 87 Mass. 280 (1862). A consolidation thereunder has been held legal, *Bishop v. Brainerd*, 28 Conn. 289 (1859); also not legal, *Kenosha, Rockford, & Rock Island R. R. Co. v. Marsh*, 17 Wis. 13 (1862); *Mowrey v. Ind. & Cin. R. R. Co.*, 4 Biss. 78 (1866); authorizing one railroad to subscribe for stock in another railroad has been held legal, *White v. Syracuse & Utica R. R. Co.*, 14 Barb. 559 (1853); also borrowing money and building branches, *Northern R. R. Co. v. Miller*, 10 Barb. 260 (1851); also reducing capital stock, *Joslyn v. Pacific Mail Steamship Co.*, 12 Abb. Pr. R. (N. S.) 329 (1872). See also *White Hall & Plattsburgh R. R. Co. v. Myers*, 16 Abb. Pr. (N. S.) 34 (1872); *State v. Accommodation Bk. of La.*, 26 La. Ann. 288 (1874); *Kenosha, Rockford & Rock Island R. R. Co. v. Marsh*, 17 Wis. 13 (1863). The extension of the line from six to seventeen miles, was held to require an unanimous acceptance in *Zabriskie v. Hackensack & N. Y. R. R. Co.*, 18 N. J. Eq. 178 (1867).

§ 502. *Dissenting stockholder's remedy against an illegal amendment.*—Where an unauthorized and illegal amendment has been accepted by a corporation, and is about to be acted upon, a stockholder has two remedies. If he has not paid his subscription, he may consider himself released from his liability to pay the subscription, or he may begin suit in equity to obtain an injunction against any action by the corporation under the amendment.¹ If the stockholder has already paid his subscription, then his only remedy is an injunction.² In Pennsylvania it has been held that the stockholder may have an injunction herein, but only until the corporation shall have purchased his interest in the corporation.³ This decision, however, has been doubted, and hardly seems consistent with well established principles, protecting persons in their rights to retain their property, except as taken from them under the power of eminent domain.⁴

§ 503. *Assent and acquiescence as a bar to the stockholder's remedy.*—A stockholder may be estopped from objecting to an amendment, by his express or implied acquiescence therein. Any acts indicating an acceptance by him of the amendment

¹ This rule is recognized and applied in most of the cases of this chapter. See also *Clearwater v. Meredith*, 1 Wall. 25, holding that the stockholder was released, and saying: "Clearwater could have prevented this consolidation, had he chosen to do so." *Nugent v. Supervisors*, 19 Wall. 241 (1873); *Champion v. Memphis, &c., R. R. Co.*, 35 Miss. 692 (1858). In England cases generally arise, releasing the subscriber, when the memorandum of association vary from the prospectus: *Stewart's Case*, L. R., 1 Ch. 574 (1866); *Webster's Case*, L. R., 2 Eq. 741 (1866); *Ship's Case*, 2 De G., J. & S. 544 (1865); *Dawes v. Ship*, L. R., 3 H. of L. 343 (1868). Cf. *Nixon v. Brownlaw*, 3 H. & N. 686 (1858); *Norman v. Mitchell*, 5 De G., M. & G. 648 (1854). See also *Dorris v. Sweeney*, 60 N. Y. 463 (1875). After a winding up has commenced, there can be no release herein. *Oakes v. Turquand* L. R., 2 H. L. 325 (1867). In opposition to this rule of law, there are some decisions holding that the subscribers' only remedy is an injunction. Were it not that the great weight of authority holds otherwise, this view would be commended as the only logical result of the law. There

is no reason why a stockholder who has not paid his subscription, should be better off than he who has met that obligation. See § 187, also *Hays v. Ottawa, &c., R. R. Co.*, 61 Ill. 422 (1871); *Pacific R. R. v. Hughes*, 22 Mo. 291 (1855); also *Martin v. Pensacola R. R. Co.*, 8 Fla. 389; *Ware v. Grand, &c., Ry. Co.*, 2 Russ. & M. 470. The plea of release, must allege acceptance by the corporation, and injury to the defendant sued on his subscription, *Hawkins v. Miss. & Tenn. R. Co.*, 35 Miss. 688 (1858).

² This remedy also is supported by a large number of the cases in this chapter. See *Stevens v. Rutland & Burlington R. R. Co.*, 29 Vt. 545 (1855); *Black v. Del. & Raritan Canal Co.*, 24 N. J. Eq. 455 (1873); *Mowrey v. Ind. & Cin. R. R. Co.*, 4 Biss. 78 (1866).

³ *Lauman v. Lebanon Valley R. R. Co.*, 30 Pa. St. 42 (1858); approved in *Slate v. Bailey*, 16 Ind. 46 (1861). Cf. *Ship v. Crosskill*, L. R., 10 Eq. 73 (1870); *Stewart v. Austin*, L. R., 3 Eq. 299 (1866), holding that the recovery back cannot be in a court of equity.

⁴ *Mowrey v. Ind. & Cin. R. R. Co.*, 4 Biss. 78 (1866).

bind him and bar his suit.¹ Acquiescence may sometimes grow out of his silence, under circumstances that called on him to dissent, if he so intended.² His assent, however, is not to be presumed, but must be proven.³

¹ Bedford R. R. Co. *v.* Bowser, 48 Pa. St. 29 (1864). Long delay may constitute a ratification herein. Gifford *v.* New Jersey R. R. Co., 10 N. J. Eq. 171 (1854). See in general, Memphis, &c., R. R. Co. *v.* Sullivan, 57 Ga. 240; Houston *v.* Jefferson College, 63 Penn. St. 428; Danbury, &c., R. R. Co. *v.* Wilson, 22 Conn. 435; Vermont, &c., R. R. Co. *v.* Vermont Cent. R. R. Co., 34 Vt. 2; Hayworth *v.* Junction R. R. Co., 13 Ind. 348 (1859); Mills *v.* Central R. R. Co., 41 N. J. Eq. 1 (1886); Zabriskie *v.* Hackensack, &c., R. R. Co., 18 N. J. Eq. 178; *Ex parte* Booker, 18 Ark. 338; Upton *v.* Jackson, 1 Flipp. C. C. 413; Goodin *v.* Evans, 18 O. St. 150.

If the stockholder subscribed after the amendment was made, he cannot complain. Eppes *v.* Miss., &c., R. R. Co., 35 Ala. (N. S.) 54 (1859); McClure *v.* People's Freight Co., 90 Pa. St. 269 (1879).

² Commonwealth *v.* Cullen, 13 Pa. St. 133 (1850); Martin *v.* Pensacola & Ga. R. R. Co., 8 Fla. 370 (1869); Owen *v.* Purdy, 12 O. St. 73 (1861). *Contra*, Hamilton Mutual Ins. Co. *v.* Hobart, 2 Gray, 543 (1854).

³ March *v.* Eastern R. R. Co., 43 N. H. 515 (1862); Prop., &c., Union Lock & Canals *v.* Towne, 1 N. H. 44 (1817); Ireland *v.* Palestine, &c., Turnpike Co., 19 O. St. 369 (1869).

CHAPTER XXIX.

JOINT-STOCK COMPANIES.

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| <p>§ 504. Definitions.
505. Statutory joint-stock companies.
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§ 504. *Definitions.—Joint-stock companies.*—A joint-stock company may be defined to be an association of persons for the purpose of business, having a capital stock divided into shares, and governed by articles of association which prescribe its objects, organization, and procedure, and the rights and liabilities of the members, except that the articles cannot release the members from their liability as partners to the creditors of the company.¹

¹ In *Hedge & Horne's Appeal*, 63 Pa. St. 273 (1869), it is defined to be "a partnership whereof the capital is divided or agreed to be divided into shares, and so as to be transferable without the express consent of all the copartners." In the statutes of Massachusetts the words "joint-stock company" are used to mean a corporation organized under the general incorporation act of the State. *Atty. Gen. v. Mercantile Ins. Co.*, 121 Mass. 524 (1877), but this is not an accurate use of the term. "The articles of association of an unincorporated joint-stock company bear the same relation to it, that the charter bears to an incorporated company. They regulate the duties of the officers, and the duties and obligations of the members of such a company among themselves; they specify the capital, limit, the duration, and define the business of the company." *Bray v. Farwell*, 81 N. Y. 600 (1880), per Earl, J. See also *White v. Brownell*, 4 Daly, 162, 193. In *Robbins v. Butler*, 24 Ill. 387, 426, 432 (1866), it is said that joint-stock companies "have none of the rights and immunities of . . . a regularly incorporated company. These stock companies are nothing more than partnerships, and every member of the company

is liable for the debts of the concern, no matter what the private arrangements among themselves may be." To the same effect see *Moore v. Brink*, 4 Hun, 402 (1875); *Skinner v. Dayton*, 19 Johns. 513 (1822); *Wells v. Gates*, 18 Barb. 554 (1854); *Keasley v. Codd*, 2 Carr. & P. 408 (1826). "The term joint-stock company appears to have originated in England, in comparatively recent times. Joint-stock companies may be said to be partnerships, or individuals associated for some specified purpose under a designated name or description, to which, by some general or special statute, when they have been formed or composed in a specified manner, some of the powers or proper attributes of a corporation have been given." *Dayton, &c., R. R. Co. v. Hatch*, 1 Disney Cin. Super. Ct. 84, 90 (1855); *Factors, &c., Insurance Co. v. Harbor, &c., Co.*, 37 La. Ann. 233, 239 (1885), speaks of a joint-stock company as "a nondescript organization, composed of the owners of certificates showing the proportion of their respective interest in its assets and liability for its obligations, and who are co-owners or proprietors in common. As no one is bound to own property in indivision, it follows that such owners who wish a division have a

A joint-stock company lies midway between a corporation and a copartnership. It is, however, to be distinguished from them,¹ and also from clubs,² from social, benevolent,³ and mutual aid⁴ organizations, and from associations formed for business purposes, but without a capital stock.⁵ A joint-stock company, although it exercises the power to issue stock, the same as a corporation, yet when organized for the purpose of transacting any lawful business, is itself a lawful mode of carrying on business.⁶

right to have that property sold, and after a liquidation of the affairs of the concern to have the residue distributed ratably among themselves." At common law a partnership may do business under any name that it chooses. See § 233. As to the effect of a deed, grant, or bequest of real estate to an unincorporated association, see *Webb v. Weatherhead*, 17 How. 576 (1854); *Gerard's Titles to Real Estate*, p. 490; *Owens v. Missionary Soc. of the M. E. Church*, 14 N. Y. 380; *Washburn on Real Prop.* vol. III, p. 264 (4th ed.); *Holmes v. Mead*, 52 N. Y. 332; *Goesele v. Bumler*, 5 McLean, 223 (1851); *German Land Association v. Scholler*, 10 Minn. 331 (1865); *Peabody v. Eastern Methodist Society in Lynn*, 87 Mass. 540 (1857); *Towar v. Hale*, 46 Barb. 361 (1866); *Dart on Vendors & Purchasers*, vol. I, p. 21 (5th ed.); *Chapin v. First, &c., Soc.*, 74 Mass. 582 (1857).

¹ It differs from a corporation in that a joint-stock company has no limited liability as regards its stockholders; it cannot sue or be sued in the name of the association; and it has no seal. It differs from a copartnership in that it is not dissolved by a transfer of stock; and each member has not the same powers of transacting business and disposing of the assets as in a partnership. See *Cox v. Bodfish*, 35 Me. 302 (1853).

² *Park v. Spaulding*, 10 Hun, 128; *Ridgely v. Dobson*, 3 Watts & S. 118; *Loubat v. Le Roy*, 40 Hun, 546; *Fleming v. Hector*, 2 Mees. & W. 172 (1836); *Re St. James Club*, 2 De G., M. & G. 383 (1852); *Ewing v. Midlock*, 5 Port. (Ala.) 82 (1837); *Todd v. Emly*, 8 M. & W. 505; *Raynell v. Lewis*, 15 M. & W. 517; *Wood v. Finch*, 2 F. & F. 447; *Cross v. Williams*, 10 W. R. 302; *Cockerel v. Aucompe*, 5 W. R. 633; *Koehler v. Brown*, 31 How. 235; *Waller v. Thomas*, 42 How. 337; *Hopkinson v. Marquis of Exeter*, 16 W. R. 266; *Gardner v. Frunatte*, 19 W. R. 256.

³ *Penfield v. Skinner*, 11 Vt. 296 (1839); *Beaumont v. Meredith*, 3 Ves. & B. 180 (1814). See also *Thomas v. Ellmaker*, 1 Parsons Sel. Eq. Cases, 98 (1844). Or Masonic Lodges. See *Ash v. Guie*, 97 Penn. St. 493 (1881).

⁴ *Lafand v. Deems*, 81 N. Y. 507 (1880); *Frits v. Muck*, 62 How. Pr. 69 (1881); *Pipe v. Bateman*, 1 Iowa, 369 (1855). Cf. *Thomas v. Ellmaker*, 1 Parsons Sel. Eq. Cases, 98 (1844); *Olery v. Brown*, 51 How. Pr. 92 (1875).

⁵ Such as Stock Exchanges. See *White v. Brownell*, 4 Daly, 162; *Clute v. Loveland, California*, (1885); *Leech v. Harris*, 2 Brews. 571 (1869); *Slate v. Chamber of Com.* 20 Wis. 63 (1865). For improving a water-power. *Troy Iron & Nail Factory v. Corning*, 45 Barb. 231 (1864). For building a school-house. *Marston v. Durgin*, 54 N. H. 347 (1874). For protecting business interests. *Caldicott v. Griffiths*, 8 Ex. 898 (1853). See also *Tenney v. New Eng. Protection Union*, 37 Vt. 64 (1864); *Abels v. McKean*, 18 N. J. Eq. 462; *Henry v. Jackson*, 37 Vt. 431 (1865); *Frost v. Walker*, 60 Me. 468 (1865).

⁶ *Townsend v. Goewey*, 19 W. R. 423. In England, a joint-stock company, organized without reference to any statute, has been held to be an usurpation and contempt of the royal prerogative. *Duvergier v. Fellows*, 5 Bing. 248 (1828); *Blundell v. Winsor*, 8 Sim. 601 (1837). In the former case the court said: "Persons who, without the sanction of the legislature, presume to act as a corporation, are guilty of a contempt of the King, by usurping on his prerogative. . . . It concerns the public that bodies, composed of a great number of persons with large disposable capitals, should not be formed without the authority of the Crown, and subject to such regulations as the King in his wisdom might deem necessary for the public safety." And again, "The scheme in

A "car trust association," or "car trust," as usually organized in this country, is in the nature of a joint-stock company.¹

§ 505. *Statutory joint-stock companies.*—There is an essential difference between a joint-stock company, as it exists at

which the parties to this action were engaged was one of those bubbles by which, to the disgrace of the present age, a few projectors have obtained the money of a great number of ignorant and credulous persons to the ruin of those dupes and their families, and by which a passion for gambling has been excited, that has been most injurious to commerce and to the morals of the people." But the modern view does not sustain this, and Pollock on Contracts, 222, clearly states that "unincorporated companies, with transferable shares, are not unlawful at common law."

¹ In an able address by Mr. Francis Rawle, before the American Bar Association in 1885, on the subject of "Car Trust Securities," the following clear statement of the character of a "Car Trust Association," or a "Car Trust," is made: "The articles of association fix the amount of the capital stock, and provide that those persons who sign the articles of association, and any others that may join it, or hold certificates of its stock, shall constitute its membership; that neither the death, insolvency, or bankruptcy of any stockholder, nor the transfer of shares, nor the admission of new members into the association, shall work its dissolution; that when a member ceases to be a stockholder, he ceases to be a member of the association, and shall not afterwards be liable on any contract, and any person purchasing a share, shall thereby become a member of the association; that only the property of the association shall be liable for its debts, and all its contracts shall contain a provision that only its funds and property shall be liable for its debts, and that no member of the board of managers, nor any stockholder, shall be so liable, personally; that its entire business shall be transacted, and all contracts shall be made, only by the board of managers, who are chosen from the stockholders and named in the articles, with a provision for filling vacancies in the board, and for removing any of its members at a meeting of the stockholders called for that purpose; that upon payment of the stock subscribed, the stockholder shall receive a certificate of his ownership; that the rolling stock, when

built, shall be delivered to a trustee named in the articles, and that this trustee shall have power to contract for the association with (usually) a special railroad company to furnish it with rolling stock upon certain specified terms.

"The board of managers of the association then purchase the rolling stock, and arrange to furnish it to the railroad company through the medium of a trustee. The latter takes the legal title to the property, executes the contract with the railroad company, receives and holds the company's obligation to pay for it, issues certificates to the persons entitled, usually in sums of a thousand dollars each, receives the periodical payments under the contract, and pays the amounts of principal and interest due to the certificate holders until the rolling stock has been fully paid for, when it becomes the property of the railroad company under the terms of the contract.

"Formerly it was the practice to pay off the principal of the certificates by successive drawings, but now it has become more common to execute the certificates in series with a fixed maturity for each, usually running from one to ten years."

A car trust company, wherein the subscribers were to have certificates representing their interest, and the rolling stock owned by the company was to be rented at a certain rental, which was to go to the subscribers until their subscriptions were repaid, and then the rolling stock was to belong to the lessee, is a joint-stock company, a mere voluntary association. *Ricker v. American Loan & Trust Co.*, 140 Mass. 346 (1885). The recent issue of Cotton Oil Trust Certificates seems to be of a somewhat similar nature, except that it is not generally supposed that they are extinguished by subsequent payment. Some of the operations of the Standard Oil Company are also said to be upon the same plan. A somewhat similar device was sustained in *Griffith v. Jewett*, 15 Week. Law Bull. 419, where many stockholders transferred their stock in trust to certain trustees and received trust certificates, therefor, the trustees having the sole power to vote and retain the stock itself.

common law, and a joint-stock company having extensive statutory powers conferred upon it by the State within which it is organized. The latter kind of joint-stock companies ~~are~~ found in England and in the State of New York. To such an extent have these statutory powers been conferred on joint-stock companies that they differ from corporations only in not having a seal, and in the members not being exempt from liability as partners for the debts of the company. Accordingly, joint-stock companies, both those of England and of New York, have been held to be corporations, although expressly declared by statute not to have that character.¹

§ 506. *Joint-stock companies may arise by implication of law.*—Joint-stock companies are generally formed by the mutual agreement and direct intent of the parties. They may, however, arise by implication of law. Thus, an ineffectual attempt at an incorporation may make the parties members, not of a corpora-

¹ For New York Statutes herein, see Sess. Laws 1854, ch. 245; Sess. Laws 1867, ch. 289; Sess. Laws 1868, ch. 290; Sess. Laws 1881, ch. 599; Sess. Laws 1858, ch. 172. See *Thomas v. Dakin*, 22 Wend. 9; *Warner v. Beers*, 23 Wend. 103; *Parmy v. Tenth Ward Bk.* 3 Edw. 395; *People v. Watertown*, 1 Hill, 616; *Bk. of Watertown v. Watertown*, 25 Wend. 686; *Willoughby v. Comstock*, 3 Hill, 389; *Leavitt v. Yates*, 4 Edw. 134; *Leavitt v. Tyler*, 1 Sandf. Ch. 207; *People v. Niagara*, 4 Hill, 20; *Boisgerard v. New York Banking Co.*, 2 Sandf. Ch. 281; *Matter of Bank of Danville*, 6 Hill, 370; *Gifford v. Livingston*, 2 Den. 380; *Case v. Mechanics' Banking Assoc.*, 1 Sandf. 693; *Leavitt v. Blatchford*, 17 N. Y. 521; 5 Barb. 9; *Culver v. Sanford*, 8 Barb. 225; *Gillett v. Moody*, 3 N. Y. 478; *Talmage v. Pell*, 7 N. Y. 328; *Tracy v. Talmage*, 18 Barb. 456; *Gillett v. Phillips*, 13 N. Y. 114; *Falconer v. Campbell*, 2 McLean, 195. The English joint-stock company is much the same. "The company has a name as an association, maintaining the identity of the body through all changes of its members; its property is divided into transferable shares, and it has conferred upon it the legal capacity to sue and be sued in the name of one of its officers, and such a suit . . . may be brought by or against a member, as well as a third person." It is a corporation though the

English statute declares it is not. *Oliver v. Liverpool & London Life & Fire Ins. Co.*, 100 Mass. 531 (1868); *aff'd sub nom. Liverpool Ins. Co. v. Mass.*, 10 Wall. 566 (1870). So also with the New York joint-stock companies. *Fargo v. Louisville, New Albany & Chicago Ry. Co.*, 6 Fed. Rep. 787 (1881); *Sanford v. Bd. of Supervisors of N. Y.*, 15 How. Pr. 172 (1858); *Waterbury v. Merchants' Union Ex. Co.*, 50 Barb. 157 (1867). As regards the liability of the members for the debts of the company, it is held to be a copartnership. *Boston & Albany R. R. Co. v. Pearson*, 128 Mass. 445 (1880); *Oliver v. Liverpool & London Life & Fire Ins. Co.*, *ubi supra*. The refusal of the legislature to call them corporations is important as cutting off the exemption of the members from liability to creditors, an exemption which, at common law, belongs to all corporations. Joint-stock companies in England have always been largely statutory. See *Van Sandau v. Moore*, 1 Russ. 391 [*441] (1826). Accordingly, in this chapter, the English decisions have not been particularly relied on. They are, however, authority on the other parts of this work, and are found throughout it. In the State of New York, the English decisions on these companies are doubtless good authority, since they exist under statutes which are much alike.

tion, but of a joint-stock company.¹ In like manner, after the charter of a corporation expires and the parties continue to do business, they do so as a joint-stock company.²

§ 507. *How a person becomes a member—Transfers.*—A person becomes a member of a joint-stock company by any act which indicates an intent to become a member on his part, and a consent or acquiescence therein by the company itself.³ He may also become a member by a transfer made to him of another member's interest, unless the articles of association restrict the right of transfer.⁴

§ 508. *Liability of members to creditors and to the company.*—A joint-stock company is, in regard to the liability of its members to creditors of the company, a partnership;⁵ its members are liable as partners;⁶ and the ordinary rules of partnership

¹ *Re Mendenhall*, 9 Bankr. Reg. 497; *Whipple v. Parker*, 29 Mich. 369, 380 (1874), and see Chapter XIII. *Cf. Foster v. Pray*, 29 Northwest Rep. 155 (Minn. 1886).

² *Nat. Bk. of Watertown v. London*, 45 N. Y. 410 (1871).

³ The formalities need be no greater than in forming an ordinary partnership. No subscription in writing is necessary. *Nat. Bk. v. Van Derwerker*, 74 N. Y. 234 (1878); *Pettis v. Atkins*, 60 Ill. 454 (1871). It is not necessary that certificates of the stock be issued in order to constitute membership. *Dennis v. Kennedy*, 19 Barb. 517 (1854); *Boston & Albany R. R. Co. v. Pearson*, 128 Mass. 445 (1880). Evidence of subscription and payment of an assessment is sufficient. *Frost v. Walker*, 60 Me. 468 (1872). But not of subscription without any participation. *Hedge & Horne's Appeal*, 63 Pa. St. 273 (1869).

⁴ Transfer of the certificate of stock has such effect, although not registered in the stock book. *Butterfield v. Beardsley*, 28 Mich. 412 (1874). Transfer may be before the certificates are issued. *Butterfield v. Spencer*, 1 Bosw. 1 (1856). But if the articles of association prohibit transfer, the transferee takes only the right to profits, not as a partner, but as an assignee. *Harper v. Raymond*, 3 Bosw. 29 (1858). A transfer does not carry dividends already declared. *Harper v. Raymond*, *ubi supra*. If a transfer is improperly allowed, the company is li-

able to the party injured. *Cohen v. Gwynn*, 4 Md. Ch. 357 (1848).

⁵ *Kellogg Bridge Co. v. United States*, 15 Ct. of Cl. 111.

⁶ *Westcott v. Fargo*, 61 N. Y. 542 (1875); *Witherhead v. Allen*, 3 Keyes, 562; *Cross v. Jackson*, 5 Hill, 478 (1843); *Skinner v. Dayton*, 19 Johns. 513 (1822); *Wells v. Gates*, 18 Barb. 554 (1854); *Boston & Albany R. R. Co. v. Pearson*, 128 Mass. 445 (1880); *Taft v. Ward*, 106 Mass. 518 (1871); *Id.* 111 Mass. 518 (1873); *Bodwell v. Eastman*, 106 Mass. 525 (1871); *Tappan v. Bailey*, 45 Mass. 529 (1842); *Cutter v. Estate of Thomas*, 25 Vt. 73 (1852); *Frost v. Walker*, 60 Me. 468 (1872); *Kramer v. Arthurs*, 7 Pa. St. 165 (1847); see also § 504. *Contra, Irvine v. Forbes*, 11 Barb. 587 (1852); *Livingston v. Lynch*, 4 Johns. Ch. 573 (1820), overruled as *dicta* by *Townsend v. Goewey*, 19 Wend. 423 (1838); *Ridenour v. Mayo*, 40 O. St. 9 (1883). In *Frost v. Walker*, 60 Me. 468 (1872), the court said: "An unincorporated joint-stock company is a mere partnership, and each member is personally liable for all its debts. It is important for the public to know, that if persons connect themselves with a company of this description, they are every one of them liable to pay the demands upon it." A member who transfers his interest is nevertheless liable for precedent debts of the association. *Morgan's Case*, 1 De G. & Sm. 750 (1849). The officers who enter into a contract for the company are

exist between the members themselves,¹ including the right to contribution as between themselves,² and also between a member and third persons.³ The member's subscription may be enforced by a suit at law.⁴ The rights and liabilities of a member depend upon the law of the place of domicile of the company itself.⁵ The rules applicable to stockholders in corporations are, by analogy, applied to members in these companies, especially as regards their defenses to subscriptions,⁶ and meetings of the company.⁷

liable thereon personally. "It is immaterial whether they be so held because they held themselves out as agents for a principal that had no existence, or on the ground that they must, under the contract, be regarded as principals, for the simple reason that there is no other principal in existence." *Lewis v. Tilton*, 64 Iowa, 220 (1884); *Fredenhall v. Taylor*, 26 Wis. 286 (1870). In enforcing the liability of members of a joint-stock company, if the parties are very numerous or unknown, they need not all be joined as defendants. *Mandeville v. Riggs*, 2 Pet. 482 (1829), rev'g *Riggs v. Swann*, 3 Cr. 188. See also *Phipps v. Jones*, 20 Penn. St. 260; *Dennis v. Kennedy*, 19 Barb. 517; *Wood v. Draper*, 24 Barb. 187; *Smith v. Lockwood*, 1 Code Rep. N. S. 319; *Birmingham v. Gallagher*, 112 Mass. 190; *Snow v. Wheeler*, 113 Mass. 179; *Pipe v. Bateman*, 1 Iowa, 369; *Marshall v. Loveless, Cam. & N.* 217; *Lloyd v. Loaring*, 6 Ves. 773; *Deems v. Albany, &c. Line*, 14 Blatch. 474. In regard to the efforts of such unincorporated associations to save themselves from liability as partners by provisions limiting their liability inserted in all contracts made with third persons, Chancellor Kent says (*Kent's Com.* Vol. III, p. 27): "It is, however, the judicial language in some of the cases that the members of a private association may limit their personal responsibility, if there be an explicit stipulation to that effect made with the party with whom they contract, and clearly understood by him at the time. But stipulations of that kind are looked upon unfavorably, as being contrary to the general policy of the law, and it would require a direct previous notice of the intended limitation to the party dealing with the company and his clear understanding of the terms of the limitation." See also *Shelford on Joint Stock Companies*, pp. 3, 4. The supposition or belief of the members, that they are not liable beyond the par value of their stock, does

not protect them from liability. *Farnum v. Patch*, 60 N. H. 294, and see § 233, note. The liability cannot be limited by a provision in the articles of association, and a mere reference to them in the contracts made. *Hess v. Werts*, 4 S. & R. (Penn.) 356 (1818). See also *Davis v. Beverly*, 2 Cr. 35. Cf. *Mandeville v. Riggs*, 2 Pet. 482. As regards the practice in bringing actions against members of an unincorporated association, see *Kneeland on Attachments*, Ch. XVI.

¹ *Bullard v. Kinney*, 10 Cal. 60 (1858).

² *Morrissey v. Weed*, 12 Hun. 491; *Skinner v. Dayton*, 19 Johns. 513 (1822).

³ His interest cannot be reached by execution. *Kramer v. Arthurs*, 7 Pa. St. 165 (1847). Acquiescence in the dealings of other members with third persons binds a member. *Penn. Ins. Co. v. Murphy*, 5 Minn. 36 (1860); *Wells v. Yates*, 18 Barb. 554 (1854). For the liability as affected by the transfer of stock, see *Smith v. Virgin*, 33 Me. 148 (1851).

⁴ If the subscription runs to the trustees personally, they may sue thereon. Otherwise all must join as plaintiffs. *Cross v. Jackson*, 5 Hill, 478 (1843). *Townsend v. Goewey*, 19 Wend. 428 (1838). It seems that a subscription to a voluntary association is enforceable by a corporation which took the place of the proposed voluntary association, where the subscriber knew of the change of plan and did not object. *City Sav. Bk. v. Whittle*, 63 N. H. 587 (1886).

⁵ *Cutler v. Estate of Thomas*, 25 Vt. 73 (1852).

⁶ That the full capital stock must be subscribed, before any subscription is collectible, see *Bray v. Farwell*, 81 N. Y. 600 (1880). *Contra Tappan v. Bailey*, 45 Mass. 529 (1842); *Boston & Albany R. R. Co. v. Pearson*, 128 Mass. 445 (1880); *Pitchford v. Davis*, 5 Mees. & W. 2 (1839). Forfeiture of stock releases the member only as to subsequent debts. *Skinner v. Dayton*, 19 Johns. 513 (1822).

⁷ Notice of the time and place must

§ 509. *Actions by members against officers and the company.*—The members may bring an action to remedy the fraud,¹ *ultra vires* acts,² and negligence³ of the trustees. In New York, a member may, by statute, sue the company, in the same manner that a stockholder in a corporation may sue the corporation.⁴

§ 510. *Dissolution.*—Where the term of existence of a joint-stock company is fixed by its articles of association, it cannot be dissolved at the instance of a member, before the expiration of that time.⁵ It may be dissolved where the enterprise becomes wholly impracticable or its attainment impossible, but not because of the misconduct of its officers.⁶ Upon dissolution the trustees of the company are bound to convert the property into cash and distribute it.⁷ In proceedings for a dissolution, all the members need not be made parties.⁸

be given. *Irvine v. Forbes*, 11 Barb. 587 (1852). The members cannot act, except in meeting assembled. The majority, however, do not rule. All must concur. *Livingston v. Lynch*, 4 Johns. Ch. 573 (1820); *Irvine v. Forbes*, *ubi supra*. *Contra*, *Waterbury v. Merchants' Union Ex. Co.* 50 Barb. 157 (1867).

¹ The other members are not proper parties. *Boody v. Drew*, 46 How. Pr. 459 (1874). An officer may be enjoined, but not removed. The suit must not be in the interest of a rival company. *Waterbury v. Merchants' Union Ex. Co.*, 50 Barb. 157 (1867). Trustees receiving gifts are liable therefor to the company. *In re Fry*, 4 Phil. Rep. 129 (1860). Cannot sell to the company. *Robbins v. Butler*, 24 Ill. 387 (1860). Treasurer may be compelled to pay over funds belonging to the company. *Sharp v. Warren*, 6 Price, 131 (1818). The trustees are liable in tort for their frauds on the company. *Dennis v. Kennedy*, 19 Barb. 517 (1854).

² A member cannot be compelled to accept the stock of another company, for his interest, a consolidation of the two having been made. *Frothingham v. Barney*, 13 Hun, 366. But he may not be able to prevent the consolidation. *McVicker v. Ross*, 55 Barb. 247 (1869).

An *ultra vires* act may be enjoined. *Abels v. McKean*, 18 N. J. Eq. 462 (1867). The members need not make good to the officers, debts paid by the latter, growing out of *ultra vires* acts. *Crum's Appeal*, 66 Pa. St. 474 (1878). But the officers

themselves are liable to third persons, *Sullivan v. Campbell*, 2 Wall. 271 (1829), and possibly the members. *Id.* If a member has not participated or acquiesced in the *ultra vires* act, he is not liable thereon. *Roberts' Appeal*, 92 Penn. St. 407 (1880). *Cf.* *Van Aernam v. Bleistein*, 102 N. Y. 355 (1886).

³ *In re Fry*, 4 Phil. Rep. 129 (1860).

⁴ Code of Civil Procedure, § 1919; *Westcott v. Fargo*, 61 N. Y. 542 (1874); *Saltsman v. Shults*, 14 Hun, 256. At common law the name is not recognized, and the suit would fail. *Habicht v. Pemberton*, 4 Sandf. 657 (1851); *Pipe v. Bateman*, 1 Iowa, 369 (1855); *Ewing v. Medlock*, 5 Port. (Ala.) 82 (1837); *Schmidt v. Gunther*, 5 Daly, 452 (1874).

⁵ See *Smith v. Virgin*, 33 Me. 148 (1851).

⁶ *Waterbury v. Mercantile Union Ex. Co.*, 50 Barb. 157 (1867).

⁷ *Frothingham v. Barney*, 13 Hun, 366; *Butterfield v. Beardsley*, 23 Mich. 412 (1874). Upon the expiration of the time for which the company was organized, it becomes dissolved, and the assets must be distributed if any one of the members insists thereon. *Mann v. Butler*, 2 Barb. Ch. 362 (1847).

⁸ Such as non-residents who cannot be reached. *Angell v. Lawton*, 76 N. Y. 540 (1879). The complainant may bring the proceeding in behalf of himself and others having a common interest with him. *Mann v. Butler*, 2 Barb. Ch. 362 (1847).

CHAPTER XXX.

STOCKHOLDERS' RIGHT TO INSPECT THE BOOKS OF THE CORPORATION.

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| § 511. Common law rights. | § 516. Allegations and form of writ. |
| 512. Common law action for damages for refusal. | 517. Right to inspect minutes of meetings of directors. |
| 513. Mandamus is the preferable remedy. | 518. Statutes giving right of inspection. |
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| 515. When it will and will not be granted. | 520. <i>Subpœna duces tecum</i> to the corporation. |

§ 511. *Common law rights*.—The stockholders of a corporation had, at common law, a right to examine, at any reasonable time, any one or all of the books and records of the corporation.¹ This rule grew out of an analogous rule applicable to public corporations and to ordinary copartnerships, the books of which, by well established law, are always open to the inspection of members.²

§ 512. *Common law action for damages for refusal*.—The legal right of a stockholder of a corporation to examine the corporate books is a right which gives him a cause of action at law for damages against the corporate officers if they refuse to allow the inspection.³ The plaintiff is entitled to nominal damages, and to

¹ Stockholders "have the right, at common law, to examine and inspect all the books and records of the corporation, at all seasonable times, and to be thereby informed of the condition of the corporation and its property." Per Redfield, J., in *Lewis v. Brainerd*, 53 Vt. 519 (1881). In the case of *Commonwealth v. Phoenix Iron Co.*, 105 Pa. St. 111 (1884), the court said: "In the absence of agreement, every shareholder has the right to inspect the accounts, a right subject to the necessities of the company, yet existing." Also, "The doctrine of the law is that the books and papers of the corporation, though of necessity kept in some one hand, are the common property of all the stockholders." The right

exists, although "its exercise be inconvenient to the bookkeepers and managers of the partnership business." In the case of *Huyler v. Cragin Cattle Co.*, 40 N. J. Eq. 392 (1885), the court said: "Stockholders are entitled to inspect the books of the company for proper purposes at proper times, and they are entitled to such inspection though their only object is to ascertain whether their affairs have been properly conducted by the directors or managers. Such a right is necessary to their protection."

² *Commonwealth v. Phoenix Iron Co.*, *supra*.

³ *Lewis v. Brainerd*, 53 Vt. 510 (1881).

such further damages as he may prove. He need not allege or prove any special reason or purpose of his desire and request to examine the books.¹

§ 513. *Mandamus is the preferable remedy.*—But an action for damages is generally totally inadequate as a remedy.² The stockholder wishes to inspect the corporate books, and does not wish damages or a law suit. Accordingly, in certain cases, upon the application of a stockholder who has been denied the privilege of examining the corporate records, it has been the practice of the courts to issue a *mandamus* to the corporate officers, commanding them to allow a specified stockholder to examine the books of the corporation.³

§ 514. *Not granted as a matter of course.*—The writ of *mandamus*, however, does not issue herein as a matter of course. It is an extraordinary remedy, to be invoked only upon special occasions. The courts do not grant the *mandamus* until it has taken into careful consideration all the facts and circumstances of the case. The condition and character of the books, the reasons for refusal by the corporation, the specific purpose of the stockholder in demanding inspection, the general reasonableness of the request, and the effect on the orderly transaction of the corporate business in case it is granted, are all considered in granting or refusing the writ. It is granted only in furtherance of essential justice.⁴

¹ Lewis v. Brainerd, 53 Vt. 510 (1881).

² In Cockburn v. Union Bk., 13 La. Ann. 289 (1858), the court said a suit for damages "might last for a long time, and petitioner suffer great loss by being debarred from an examination" of the books. "He does not ask for damages, but for the exercise of a right. If he has the right, he ought to have the exercise of it as soon as possible; for the deprivation of his right cannot, perhaps, be accurately estimated in damages. It may be many years before the amount of the damage can be known."

³ "It would seem, from the weight of authority and in reason, that a shareholder is entitled to *mandamus* to compel the *custos* of corporate documents to allow him an inspection and copies of them, at reasonable times, for a specified and proper purpose, upon showing a refusal on the part of the *custos* to allow it, and not

otherwise." Commonwealth v. Phoenix Iron Co., *supra*; s. c. 6 Atl. Rep. 75 (1886), explaining the method of procedure, and holding that the applicant need not apply to a court of equity. The old rule that *mandamus* will issue only for a public purpose is no longer a rule of law, so as to prevent its use herein. Commonwealth, &c., *supra*, questioning King v. Bk. of Eng., 2 B. & Ald. 620 (1819); and King v. London, &c., Co., 5 B. & Ald. 899 (1822). See also King v. Clear, 4 Barn. & Cr. 899 (1825).

⁴ "The application is addressed to the sound discretion of the court." The reasons for granting it "should be clear and cogent. . . . To hold that every person who shows himself to be a holder of stock is at liberty to demand an examination of the transfer books, when, and as often as he pleases, and if refused, to apply for a writ of *mandamus* to enforce an absolute right, would be to establish a rule highly

§ 515. *When it will and will not be granted.*—It will not be granted to gratify curiosity, nor to aid the stock market speculations of the stockholders.¹ Either some property rights of the stockholder must be involved, or some controversy exist, or some specific and valuable interest be in question, to settle which an inspection of the corporate records becomes necessary.² It is

prejudicial to the interests of all corporations and their stockholders. . . . The power of the court should be exercised in such cases with great discrimination and care." *People v. Lake Shore & M. S. R. R. Co.*, 11 Hun, 1 (1877); *aff'd, sub nom. Re Sage*, 70 N. Y. 220 (1877). See also *People ex rel. Field v. Northern Pac. R. R. Co.*, 50 N. Y. Super. Ct. 456 (1884); s. c., 18 Fed. Rep. 471. "Discretion in these matters should be exercised in a reasonable manner, and subject to precedent." *Reg. v. Wilts. & Berks. Canal Nav.*, 29 L. T. 922 (1874).

¹ The writ will not be "granted to enable a corporator to gratify idle curiosity." *People v. Walker*, 9 Mich. 328 (1861). "The interests of all the corporators require that the writ shall not go at the caprice of the curious or suspicious." *Commonwealth v. Phoenix Iron Co.*, *supra*. "Courts should guard against all attempts by combinations to use its writ of *mandamus* to accomplish their personal or speculative ends." *People v. Lake Shore & M. S. R. R. Co.*, *supra*. "Nor will the court grant 'a mere wrecking petition to ruin a going concern.'" *In re West Devon, &c., Mine*, L. R. 27 Ch. D. 106 (1884).

² Thus, where there had been no dividends for nine years, and the officers were partners in a competing concern, and refused to allow inspection, it was granted in order to enable the applicant to ascertain whether the real facts justified an action for fraud on the part of the officers. *Commonwealth v. Phoenix Iron Co.*, *supra*. Granted also to allow applicant to ascertain whether a by-law existed entitling him to an office by promotion. *Reg. v. The Saddlers' Co.*, 10 W. R. 77 (1861). Mismanagement and intent to bring suit need not be alleged. "Offentimes frauds are discoverable only by examination of the books by an expert accountant." *Huyler v. Cragin Cattle Co.*, *supra*. It is granted also to a stockholder who has a suit or controversy with a party other than the corporation itself. *Mayor of Southampton v. Graves*, 8 T. R.

590 (1800); *Rex v. Newcastle*, 2 Strange, 1223 (1787). It has been granted to enable a stockholder to see the discount book, although there is no suit between him and the corporation, and no intent to bring one. *Cockburn v. Union Bk.*, 13 La. Ann. 289 (1858). At an early day, however, it was held that "the members have no right, on speculative grounds, to call for an examination of the books and muniments in order to see if, by possibility, the company's affairs may be better administered than they think they are at present. If they have any complaint to make, some suit should be instituted, some definite matter charged, . . . or there should be some particular matter in dispute between members, or between the corporation and individuals in it; there must be some controversy, some specific purpose, in respect of which the examination becomes necessary." *King v. The Merchant Tailors' Co.*, 2 Barn. & Ad. 115 (1832). The applicant must allege the extent of his interest, also wherein his object of inspection is just and useful. *Hatch v. City Bk. of New Orl.*, 1 Rob. (La.) 470 (1842). The case of *State v. Bienville Oil Works*, 28 La. Ann. 204 (1876), states that the two preceding cases "failed through want of precision and definiteness in stating some well defined purpose, some reasonable cause, and showing that they had some interest in the matter." A charter provision that the corporate powers "shall be exercised by a board of directors," is immaterial herein. *Id.* Where a reduction of capital stock is contemplated, a large stockholder has a right to inspection to ascertain whether the business is being "prudently and profitably" carried on. *Id.* Not granted to allow applicant, a director, to inspect and make entries. *Rosenfield v. Einstein*, 46 N. J. L. 479 (1884). General purpose of ascertaining "the condition of the company" held insufficient. *People v. Walker*, 9 Mich. 328 (1861). The stockholder may take memoranda or a list of the stockholders. *Commonwealth v. Phoenix Iron Co.*, 105 Pa.

doubtful even whether it would issue in order to enable the applicant to ascertain who are stockholders, with a view to canvassing their votes for an election.¹

§ 516. *Allegations and form of writ.*—The writ should run to the person or officer who has control of the records.² The stockholder may make the inspection through an agent, and may have the aid of an interpreter, attorney, or expert.³ The request to inspect the books, for refusal of which the *mandamus* is asked, must be alleged to have been made at a proper time and place, and of the proper person, and to have been refused.⁴ The application should also state what information the applicant needs, and what books of the corporation he wishes to inspect.⁵

§ 517. *Right to inspect minutes of meetings of directors.*—It would take a very strong case to induce a court to issue a *mandamus* commanding the corporate officers to allow a stockholder to inspect the minutes of the meetings of the directors.⁶ The success of the corporate enterprise depends frequently upon the secrecy of the plans of the directors. In connection with litiga-

St. 111 (1884); *Cotheal v. Brower*, 5 N. Y. 562 (1851); *aff'g Brower v. Cotheal*, 10 Barb. 216 (1850).

¹ *Mandamus* was granted to a stockholder who wished to persuade other stockholders not to appeal a suit in which he was interested adversely to the corporation, the defeated party. *Reg. v. Wilts. & Burks. Canal Nav.*, 29 L.T. 922 (1874). See also *State v. Lake Shore & M. S. R. R. Co.*, 11 Hun, 1 (1877).

² "The writ shall be directed to him who is to do the thing required to be done." A director may demand inspection though hostile to the corporation. *People v. Throop*, 12 Wend. 181 (1834).

³ May inspect through his duly authorized agent. *State v. Bienville Oil Works Co.*, 28 La. Ann. 204 (1876). See also § 519, n. 2.

⁴ The stockholder must first apply to the proper corporate officer having authority to grant inspection. *King v. Prop. of the Wilts. & Burks. Canal Nav.*, 3 Ad. & El. 477 (1835). And must state to him the reason why he desires inspection. *Id.* Also *King v. Clear*, 4 Barn. & Cr. 899 (1825); *People v. Walker*, 9 Mich. 328 (1861).

⁵ *Morgan's Case*, L. R. 28 Ch. D. 620

(1884). This case also states that in England it is customary for many banking companies to insert in their constitutions a provision forbidding the inspection of customers' accounts by shareholders or creditors.

⁶ "It is highly proper that an inspection of the books containing the proceedings of the directors should be obtained on special occasions and for special purposes; . . . but the proposed daily and hourly inspection and publication of all their proceedings would be tantamount to admitting the presence of strangers at all their meetings, and would probably, ere long, be found very prejudicial to the shareholders." *Queen v. Mariquita Mining Co.*, 1 Ell. & Ell. 289 (1858). "A private stockholder of an incorporated company has no right to have access to the minutes of the proceedings of the directors unless that right is expressly given by the charter, and consequently and of necessity he must remain ignorant of their action until they choose to make that action known." *Ala. & Fla. R. R. Co. v. Rowley*, 9 Fla. 508, 514 (1861). See also *Lindley on Partn.*, 4th ed., 809.

tions, the rule, of course, is different; but, aside from this, it seems that a stockholder is not entitled to a *mandamus* to allow him to inspect the minutes of the directors' meetings. The same rule would seem to apply to miscellaneous questions asked of the directors at stockholders' meetings.

§ 518. *Statutes giving right of inspection.*—The right to inspect corporate records is frequently given to stockholders by statutory provisions. Sometimes this statutory right extends only to the corporate transfer book.¹ Sometimes it includes all corporate records.² Frequently the charter itself states that the stockholder shall have certain rights of inspection. In England the Companies Act regulates specifically the stockholders' right of inspection, and provides for a committee of investigation in behalf of the stockholders whenever an investigation is desired by them.³

§ 519. *Orders to corporation to allow inspection.*—An inspection of corporate records is often desired in connection with an action which is pending in the courts, and it has been the practice of the courts to grant applications for this purpose.⁴ The order to

¹ In New York, see 1 R. S. ch. XVIII, title 4, § 1, applying to all corporations. Construed in *Cotheal v. Brower*, 5 N. Y. 562 (1851); *People v. Pacific Mail Steamship Co.*, 50 Barb. 280 (1867); 1 R. S. ch. XVIII, title 2, § 45, for moneyed corporations; Laws, 1842, ch. 165, for transfer agents in this State of foreign corporations; construed in *People v. Lake Shore & M. S. R. R. Co.*, 11 Hun, 1 (1877); *People, ex rel. Field v. Northern Pacific R. R. Co.*, 50 N. Y. Super. Ct. R. 456 (1884); s. c., 18 Fed. Rep. 471; Laws of 1848, § 25, for manufacturing corporations for New Jersey. See Revision of 1877, p. 183, § 36; *Huyilar v. Cragin Cattle Co.*, 40 N. J. Eq. 392 (1885); Ind. R. S. (1881), §§ 3010–3011. A delay of one day in allowing the inspection, owing to the absence of the person having charge of them, does not cause the penalty to attach. *Kelsey v. Pfandler, &c., Co.*, 24 N. Y. Week. Dig. 295 (1886).

² Rev. Stat. of Ohio (1886), § 3312; California, Civil Code, §§ 377, 378; Penal Code, 565; R. I. Pub. Stat. ch. 153, § 21, & ch. 158, § 24 (1882); Mich. Gen. Stat. § 3173, for banks. See also Colorado Gen. Stat., 1882, § 249; Mo. R. S., 1879, §§ 720, 721; Vt. R. Laws, 1880, §§ 3294–

3295; Mass., 1860, ch. 68, § 10; Ill. R. S., 1874, ch. 32, § 13. The pleading in a cause of action arising under a statute herein must clearly bring the case within the statute. *Lewis v. Brainerd*, 53 Vt. 510 (1881). That the officer had notice of plaintiff's stockholdership must be alleged. *Williams v. College Corner & Richmond Gravel Road Co.*, 45 Ind. 170 (1873). The purpose of the inspection need not be stated to the officer. *Lewis v. Brainerd*, 53 Vt. 510 (1881). Cf. *Queen v. Undertakers of the Grand Canal*, 1 Ir. L. R. 337. *Mandamus* lies to enforce the statutory right of inspection. *People v. Pacific Mail Steamship Co.*, 50 Barb. 280 (1861). The common law right of inspection remains, although a special statutory right is also given. *People v. Lake Shore & M. S. R. Co.*, *supra*.

³ 25 & 26 Vict. c. 89, Table A, No. 78, and Nos. 60 & 86.

⁴ "In the case of existing actions these motions seem to have been first introduced with respect to court rules." The evidence sought must be directly material to the cause. *Rex v. Newcastle*, 2 Strange, 1223 (1737); *Rex v. Babb*, 3 Term R., 579 (1790). See also *Walburn v. Ingilby*, 1 Myl. & K. 61 (1832), where

allow an inspection may be made at any stage of the action. A stockholder has this right to aid him in suits with strangers, and his right herein is more extensive than the rights of the other party to the action.¹ The right also exists in suits by or against the corporation itself.² It will not be allowed, however, for the purpose of fishing out a defense.³ In New York this right of inspection by order is regulated by statute.⁴

§ 520. *Subpœna duces tecum to the corporation.*—The right of a stockholder to compel a corporation to produce in court the corporate records has been the subject of some controversy. It has been held that a *subpœna duces tecum* will not always lie herein, but that an order to the corporation to allow an inspection is the proper remedy.⁵ This right, also, in New York, is regulated by the Code of Civil Procedure.⁶

the order was to a third person having charge of the books. "The courts of common law may also make an order for the inspection of writings in the possession of one party to a suit in favor of the other." Greenleaf's Ev., vol. I, § 559. An article of the company taking away the right of inspection does not prevent a rule issuing requiring its allowance in pending litigation. *Hall v. Connell*, 3 Younge & Col. 707 (1840). The rule applies to joint-stock companies. *Woods v. De Figanieri*, 1 Rob. 681. In the Federal courts the right is statutory. 1 U. S. Stat. at Large, 82.

¹ Strangers have no more right to demand inspection of the books of a corporation, during litigation, in which the corporation is not interested, than they have to demand a similar right of any other person. *Mayor of Southampton v. Graves*, 8 T. R. 590 (1800), overruling earlier cases. See also *Opdyke v. Marble*, 44 Barb. 64 (1864); *Morgan v. Morgan*, 16 Abb. Pr. N. S. 291 (1874).

² *King v. Travannion*, 2 Chitty, 366 (1818); *Swansea Vale Ry. Co. v. Budd*, L. R. 2 Eq. Cas. 274 (1866). The affidavit to obtain the order must show that the information sought is essential. *Imperial Gas Co. v. Clarke*, 7 Bing. 95.

The officers may be orally examined by the court with reference to where the books are. *Lacharme v. Quartz Rock Mariposa Gold Min. Co.*, 1 Hurl. & Colt. 184 (1862). They may be required to make affidavits. *Ranger v. Great, &c.*, R. R. Co., 4 De G. & J. 74 (1859); *Re Barton*, 31 L. J. Q. B. 62 (1861). Such inspections may be through agents. *Bonnarcht v. Taylor*, 1 J. & H. 383 (1861); *Draper v. Manchester, &c.*, R. R. Co., 7 Jur. N. S., pt. I, 86 (1861). But see *In re West Devon, &c.*, Mine, L. R. 27 Ch. D. 106 (1884).

³ *Birmingham, Bristol & Thames Junction Ry. Co. v. White*, 1 Q. B. 282. See also *Credit Co. v. Webster*, 53 L. T. Rep. 419 (1885).

⁴ Code of Civil Proc., §§ 803-809. See *Boorman v. Atlantic & Pacific R. R. Co.*, 78 N. Y. 599 (1879); *Ervin v. Oregon Ry. & Nav. Co.*, 22 Hun, 566 (1880); *Johnson v. Consol. Silv. Min. Co.*, 2 Abb. Pr. N. S. 413; *Walker v. Granite Bk.*, 19 Abb. 111; *Thompson v. Erie Ry. Co.*, 9 Abb. N. S. 230.

⁵ *La Farge v. La Farge Fire Ins. Co.*, 14 How. Pr. 26 (1857); *Cent. Natl. Bk. v. White*, 37 N. Y. Super. Ct. 297 (1874).

⁶ Code of Civil Proc., §§ 868, 869.

CHAPTER XXXI.

LIENS OF THE CORPORATION ON STOCK FOR THE STOCK- HOLDER'S DEBTS TO THE CORPORATION.

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| <p>§ 521. No lien at common law.</p> <p>522-24. A lien may be created by statute, by charter, or by by-law.</p> <p>525. What phrases in charters or statutes will or will not authorize the corporation to create or enforce a lien on stock.</p> <p>526. The lien, when established, covers all the stockholders' shares and dividends.</p> <p>527. The lien protects the corporation</p> | <p style="text-align: right;">as to all the debts due to it from the shareholders.</p> <p>§ 528. No lien for the debts of an unrecorded transferee.</p> <p>529. The lien can be enforced for the benefit of the corporation only.</p> <p>530. Methods of enforcing the lien.</p> <p>531. The corporation may waive its lien.</p> <p>532. The lien as affected by transfers and notice.</p> <p>533. The lien on national bank stock.</p> |
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§ 521. *No lien at common law.*—Corporations, both in this country and in England, frequently possess and exercise a lien on a shareholder's stock for debts due from that shareholder to the corporation, and the reports abound in cases which define and illustrate the principles of law which govern the lien. In this chapter it is proposed to consider the origin of the lien; the extent to which it may be exercised and enforced; the waiver of it by the corporation; and its effect generally upon the transfer of shares. It is clear that at the common law a corporation has no lien upon the shares of its stockholders for debts due from them to the company.¹ The policy of the common law, especially of

¹ *Massachusetts Iron Co. v. Hooper*, 7 Cush. 183 (1851); *Bates v. New York Insurance Co.*, 3 Johns. Cas. 238 (1802); *Steamship Dock Co. v. Heron's Admx.*, 52 Penn. St. 280 (1866); *Merchant's Bank v. Shouse*, 102 Id. 488 (1883); *Fitzhugh v. Bank of Shepherdsville*, 3 Monroe, 126 (1825); *Williams v. Lowe*, 4 Neb. 382, 398 (1876); *Dana v. Brown*, 1 J. J. Marsh. 304 (1829); *Heart v. State Bank*, 2 Dev. Eq. (N. C.) 111 (1831); *Farmers, &c. Bank v. Wasson*, 48 Iowa, 336 (1878); *People v. Crockett*, 9 Cal. 112 (1858); *Sargent v. Franklin Insurance Co.*, 8 Pick. 90 (1829); *Neale v. Janney*, 2 Cranch C. C. 188 (1819); *McMurrich v. Bond Head Harbour Co.*, 9 U. C. Q. B. 333 (1852). *Of. Weston's Case*, L. R. 4 Chan. 20 (1868). The earliest reported case in which the question of the lien of the corporation upon the stock of a shareholder is considered seems to be *Gibson*, assignee of *Evans v. Hudson's Bay Company*, MS. Rep. Michael, 12 Geo. I (1726); 7 Viner's Abridgment (2d London ed.), 125. In this case the Chancellor expressly declined, after hearing the argument, to decide whether a by-law creating such a lien was valid, but expressed the opinion that it was not. The report is a poor one, but it can be gathered from it that the judges did not doubt that, in the absence of the by-law, there was no lien at common law. So also in the case

the earlier common law, was to discountenance secret liens, upon the ground that they hindered trade and restricted the safe and speedy transfer of property. It was upon this theory that the courts refused to enforce a lien upon shares against a *bona fide* purchaser of stock in a corporation.

§ 522. *A lien may be created by statute, by charter, or by by-law.*—Such a lien as this in favor of the corporation may be created by statute,¹ by charter,² and the weight of authority holds

of shares in the Provincial Bank of Ireland, *Pinkett v. Wright*, 2 Hare's Chan. 120 (1842), it was held, having reference to the deed of association, that the bank, in order to establish its right to a lien of the shares of a stockholder for a debt due from that shareholder to the bank, must show a special contract to that effect and that, in the absence of such a contract, the bank, in dealing with its stockholder, was in no better position than in dealing with a stranger. In *Byrne v. Union Bank of Louisiana*, 9 Rob. (La.) 433 (1845), it was held, in case of a refusal by the bank to transfer the stock of a shareholder who had sold it and applied for the transfer to his vendee, upon the ground that the shareholder was largely indebted to the bank, that the bank was liable in damages, and that, where the stock had depreciated since the request for the transfer had been made, the measure of damage is the difference between its value at that time and at the time of the trial. *s. v.*, *Hussey v. Manufacturers & Mechanics Bank*, 10 Pick. 415 (1830, Shaw, C. J.); *Byron v. Carter*, 22 La. Ann. 98 (1870). In *Bank of Holly Springs v. Pinson*, 58 Miss. 421 (1880), it seems that the bank had enacted a by-law to the effect that "the stock of this company shall be assignable only on the books of the company, and no transfer of any stock shall be made by any stockholder who shall be indebted to the company, and certificates of stock shall contain upon them notice of this provision." Certificates of stock having been repeatedly issued which did not contain any such notice it was held that, as to the holder of a certificate not having upon its face notice of the by-law, the bank could assert no lien upon the stock, and that, as to all persons not members of the corporation, the uniform issue of certificates not having the notice must be regarded a repeal of the by-law, or as he making of a new by-law repealing that providing for the lien. In *Vansands*

v. Middlesex County Bank, 26 Conn. 144 (1857), where neither the charter of the bank nor the by-laws contained any provision which authorized the assertion of a lien, but where the certificates were issued to each shareholder, making the stock transferable, "subject, nevertheless, to his indebtedness and liability at the bank, according to the charter and by-laws of said bank," it was held that the provision in the certificate with regard to the lien was binding on the shareholder by his acceptance of the certificate, and that such an acceptance was equivalent to an agreement that the stock should be subject to the lien. In New York the rule that there is no lien at common law, is applied to banking corporations. *Bank of Attica v. Manufacturers, &c. Bank*, 20 N. Y. 501 (1859), and to corporations formed under the general manufacturing companies act. *Driscoll v. West Bradley, &c. Manfg. Co.*, 59 Id. 96 (1874).

¹ *Pittsburg, &c. R. R. Co. v. Clarke*, 29 Penn. St. 146 (1857); *First National Bank v. Hartford, &c. Ins. Co.*, 45 Conn. 22 (1877); *Presbyterian Congregation v. Carlisle Bank*, 5 Penn. St. 345 (1847); *Rogers v. Huntington Bank*, 12 Serg. & R. 77 (1824); *National Bank v. Watson-town Bank*, 105 U. S. 217 (1881). In New York a statute gives railway corporations a lien upon the stock for the amount of the unpaid calls. New York Session Laws, 1881, chap. 468, § 12.

² *Bradford Banking Co. v. Briggs*, L. R. 31 Chan. Div. 19 (1885); *s. c.*, 53 L. T. Rep. (N. S.) 846; reversing *s. c.*, L. R. 29 Chan. Div. 149 (1885); *Union Bank of Georgetown v. Laird*, 2 Wheat. 390 (1817); *Stebbins v. Phoenix Fire Ins. Co.*, 3 Paige, 350 (1832); *Reese v. Bank of Commerce*, 14 Md. 271 (1859); *Brent v. Bank of Washington*, 10 Peters, 596 (1836); *German Security Bank v. Jefferson*, 10 Bush, 326 (1874); *Arnold v. Suffolk Bank*, 27 Barb. 424 (1857); *Leggett v. Bank of Sing Sing*, 24 N. Y. 283

that it may be created by a by-law.¹ With respect to the right of a corporation to enact a by-law creating such a lien, it may be said that in the greater number of jurisdictions it is unquestionably held that such a by-law is valid and binding upon all persons who buy or transfer the shares, and this is the older rule both here and in England, as the citation of authority shows. There is, nevertheless, strong authority for the rule that such a by-law cannot create a lien on the stock so as to bind a *bona fide* purchaser, or other person into whose hands the shares may come, to whom actual knowledge of the by-law cannot be imputed.

Such is the rule in New York,² Louisiana,³ Massachu-

(1862); *Bank of Utica v. Smalley*, 2 Cowen, 770 (1824); *Farmers Bank of Maryland v. Iglehart*, 6 Gill, 50 (1847); *Bohmer v. City Bank of Richmond*, 77 Va. 445 (1883); *Hodges v. Planters Bank*, 7 Gill & J. 306, 310 (1835); *Sabin v. Bank of Woodstock*, 21 Vt. 353 (1849); *Cross v. Phenix Bank*, 1 R. I. 39 (1840). Where the charter of a bank provides that "no part of the capital stock shall be sold or transferred except by execution or distress, or by administrators or executors, until the whole amount thereof shall have been paid in," a contract to transfer shares in the bank, not falling within the exception, made and to be carried into execution when but fifty per cent. has been paid in, is illegal and void. *Merrill v. Cole*, 15 Me. 428 (1839). *Cf. Cohn v. Bank of St. Joseph*, 70 Mo. 262 (1879).

¹ *Knight v. Old National Bank*, 3 Clifford, 429 (1871); *McDowell v. Bank of Wilmington & Brandywine*, 1 Harr. (Del.) 27 (1832); *Bank of Holly Springs v. Pinson*, 58 Miss. 421 (1880); *St. Louis Perpetual Insurance Co. v. Goodfellow*, 9 Mo. 149 (1845); *Mechanics Bank v. Merchants Bank*, 45 Mo. 513 (1870); *Spurlock v. Pacific R. R. Co.*, 61 Mo. 319 (1875); *In re Bachman*, 12 Nat. Bank. Reg. 223 (1875); *People v. Crockett*, 9 Cal. 112 (1858); *Pendegast v. Bank of Stockton*, 2 Sawyer, 108 (1871); *Lockwood v. Mechanics National Bank*, 9 R. I. 308 (1869); *Cunningham v. Alabama, &c. Trust Co.* 4 Ala. (N. S.) 652 (1843); *Geyer v. Western Insurance Co.*, 3 Pittsb. 41 (1867); *In re Dunkerson*, 4 Biss. 227 (1868); *Young v. Vough*, 23 N. J. Eq. 325 (1873); *Brent v. Bank of Washington*, 10 Peters, 596, 615 (1836); *Child v. Hudson's Bay Co.*, 2 P. Wms. 207 (1723); *Planters, &c. Ins. Co. v. Selma Savings*

Bank, 63 Ala. 585 (1879). *Cf. Heart v. State Bank*, 2 Dev. (Eq.) N. C. 111 (1831); *Farmers, &c. Bank v. Wasson*, 48 Iowa, 336, 340 (1878). In *Tuttle v. Walton*, 1 Ga. 43 (1846), it was said that as between the corporators themselves such a by-law will be held valid.

² *Driscoll v. West Bradley, &c. Co.*, 59 N. Y. 96 (1874); *Bank of Attica v. Manufacturers Bank*, 20 Id. 501 (1859). In the Matter of the Long Island R. R. Co., 19 Wend. 37 (1837); *Rosenback v. Salt Spring National Bank*, 53 Barb. 495 (1868); *Conklin v. Second National Bank*, Id. 512 (1868); s. c., aff'd, 45 N. Y. 655 (1871). In the case last cited it was held that not even where the certificate of stock contained a provision that the stock was not transferable until all the liabilities of the stockholder to the bank were paid, did the bank acquire a lien upon the shares for the subsequent indebtedness of the shareowner. And all the New York decisions proceed upon the broad ground that the policy of the law is to protect a *bona fide* vendee of shares of stock against secret or equitable claims thereto on behalf of one who has induced the vendor with the *indicia* of ownership; that accordingly a lien can be created by a by-law, only when there is an express warrant of authority in the charter or by statute; and that a power in the corporation to abridge the right of transfer by such a by-law will not be inferred from a statutory provision, unless it cannot otherwise have efficacy, and unless it present so strong a probability of intention that the contrary cannot be supposed. *Cf. Leggett v. Bank of Sing Sing*, 24 N. Y. 283 (1862); *McCready v. Ramsay*, 6 Duer, 574 (1857); *Arnold v. Suffolk Bank*, 57 Barb. 424.

³ *Bryon v. Carter*, 22 La. Ann. 98

setts,¹ Alabama,² Pennsylvania,³ California,⁴ and possibly in some other States.⁵

It is also the rule declared by the Supreme Court of the United States in cases that involve the right of the national banks to enact such by-laws.⁶ Upon the whole, it may be said, that the question whether a corporation may, by by-law, create a lien in its own favor upon the shares of its stockholders, for debts due by them to the corporation, is not settled. In the greater number of jurisdictions, such a by-law is sustained as valid. In several of the State courts, however, whose judgments are entitled to the highest consideration, and by the Supreme Court of the United States, upon grounds which accord best with a broad public policy, these by-laws are held invalid as against a *bona fide* purchaser for value and without notice.

§ 523. In Pennsylvania it is the statutory rule, that the transfer of shares of stock in a railway corporation, can be made only upon payment of any indebtedness that may exist on the part of the shareholders who seek to transfer, unless the lien is waived by the corporation.⁷ And there are similar statutes in many other States.⁸ In New Hampshire, liens upon shares are for-

(1870); *Petot v. Johnson*, 33 Id. 1286 (1881). *Cf.* *New Orleans National Banking Association v. Wiltz*, 4 Woods, 43 (1881); s. o., 10 Fed. Rep. 330.

¹ In *Nesmith v. Washington Bank*, 6 Pick. 324 (1828), the court doubted whether a by-law could under any circumstances create a lien on the shares as against the creditors of the shareowner, but do not decide the point. In *Sargent v. Franklin Insurance Co.*, 8 Pick. 90 (1829), there is a somewhat decided ground taken against the validity of any by-law which tends to limit the free transfer of shares. In *Plymouth Bank v. Bank of Norfolk*, 10 Pick. 454 (1830), Chief Justice Shaw seems to doubt the validity of a by-law giving the bank a lien on its own stock.

² *Planters, &c. Mutual Ins. Co. v. Selma Savings Bank*, 63 Ala. 585 (1879).

³ In *Steamship Dock Co. v. Heron's Admx.*, 52 Penn. St. 280 (1866), Thompson, J., says: "Whether a mere by-law would be sufficient to create a lien on stock for a general balance due the company in case of trading, manufacturing, or other corporations not engaged in loaning money, seems not only to be doubted, but generally denied. Certainly I think

it would not be unless notice of the by-law were brought home to a purchaser of stock before the purchase." *Cf.* *Merchants Bank v. Shouse*, 102 Penn. St. 488.

⁴ *Anglo-Californian Bank v. Grangers Bank of California*, 63 Cal. 359.

⁵ *Carroll v. Mullanphy Savings Bank*, 8 Mo. App. 249 (1880); *Evansville National Bank v. Metropolitan Natl. Bank*, 2 Biss. 527 (1871); *Lee v. Citizens Natl. Bank*, 2 Cin. Super. Ct. 298 (1872). *Cf.* *Neale v. Janney*, 2 Cranch C.C. 188 (1819).

⁶ *Bank v. Lanier*, 11 Wallace, 369 (1870); *Bullard v. Bank*, 18 Id. 589 (1873). Those cases, therefore, which have held that such a by-law, enacted by the national banks, is valid and enforceable against a *bona fide* purchaser of the share, must be regarded as overruled. *Vide* § 525, *infra*.

⁷ *Pittsburgh, &c., R. R. Co. v. Clarke*, 29 Penn. St. 146 (1857); *Rogers v. Huntington Bank*, 12 Serg. & R. 77 (1824). *Cf.* *Everhart v. West Chester R. R. Co.*, 28 Penn. St. 339 (1857).

⁸ *Ryder v. Alton, &c., R. R. Co.*, 13 Ill. 516 (1851); *Allen v. Montgomery R. R. Co.*, 11 Ala. 437, 451 (1847); *Gaff v. Flesher*, 33 Ohio St. 107 (1877).

bidden by statute.¹ When a lien is expressly given to the corporation by its charter or by statute, all persons dealing with the corporation are affected by it, and must take notice of it.² A statutory lien need not be set out in the certificate in order to bind the parties to a transfer.³ And where the lien is not authorized by the charter or by statute, the mere declaration of its existence in the certificate will not avail against a *bona fide* purchaser.⁴ In general, however, it is the rule that all persons must take notice of a lien given to the corporation by charter, or articles of association, or statute, while a lien given by by-law must have been actually brought to the notice of the party sought to be charged by it.⁵ A clause in a charter, declaring that debts due from the stockholders must be paid before a transfer will be allowed, is sufficient to create a lien on the stock, without other action on the part of the corporation.⁶ And so, also, a power conferred by the charter upon the directors, to refuse a transfer so long as the shareholder, who wishes to transfer is indebted to the corporation, when exercised by the corporate management, supports the lien.⁷

It has been held that a lien may be created by special agreement among the shareholders.⁸ And even that a mere usage of a corporation not to transfer shares while the owner is indebted to the corporation, is sufficient to create a lien on stock, valid

¹ By the statute of 1849, Laws of N. H., chap. 860, § 2, it is enacted that "the free sale of shares in the stock of any corporation in this State by the owners thereof, shall not be in any way or manner restricted by the by-laws of such corporation, and all such by-laws heretofore or hereafter made, shall be deemed and taken to be absolutely void." Cf. Hill v. Pine River Bank, 45 N. H. 300, 309 (1864).

² Bishop v. Globe Company, 135 Mass. 132 (1883); Union Bank of Georgetown v. Laird, 2 Wheat. 390 (1817); Bohmer v. City Bank of Richmond, 77 Va. 445 (1883); Downer's Admr. v. Zanesville Bank, Wright (Ohio), 477 (1833); Grant v. Mechanics Bank, 15 Serg. & R. 140 (1826); St. Louis Perpetual Life Insurance Co. v. Goodfellow, 9 Mo. 149 (1845); Bank of Utica v. Smalley, 2 Cowen, 770 (1824); Rogers v. Huntington Bank, 12 Serg. & R. 77 (1824); Sewall v. Lancaster Bank, 17 Id. 285 (1828). Cf. Steb-

bins v. Phoenix, &c., Insurance Co., 3 Paige, 350 (1832).

³ McCready v. Rumsey, 6 Duer, 594 (1857). Cf. Hoffman Steam Coal Co. v. Cumberland Coal & Iron Co., 16 Md. 456.

⁴ Conklin v. Second National Bank, 45 N. Y. 655 (1871). But in Vansands v. Middlesex County Bank, 26 Conn. 144 (1857), it is held that a statement on the face of the certificate of stock, that it is issued subject to all debts due from the owners to the corporation, will bind a transferee, as a qualification or restriction of the transferrer's title, and that, too, although no charter provision or by-law authorizes such a lien on the stock.

⁵ Morawetz on Corp. (2d edition), § 203, and cases cited.

⁶ Farmers' Bank of Maryland Case, 2 Bland's Chan. 394 (1830).

⁷ Arnold v. Suffolk Bank, 27 Barb. 424 (1857).

⁸ Vansands v. Middlesex County Bank, 26 Conn. 144 (1857).

between the corporation and its shareholders, and one which will certainly bind a shareholder who borrows money with knowledge of it.¹

§ 524. It is a salutary rule, that a lien created by by-law can bind only those who take the stock with notice of the by-law. This is because by-laws do not of themselves impart or convey notice.² So, too, a by-law enacted subsequently to a transfer,

¹ *Waln's Assignees v. Bank of North America*, 8 Serg. & R. 73, 88 (1822); s. c. 11 Am. Dec. 575. In the opinion in this case, at page 88, it is vigorously said:

"Was this regulation of the bank, this usage to retain, this course of dealing between the bank and her customers, unquestionably known as it was to Mr. Waln, binding on him? That such a by-law was within the power of the bank, a by-law imposing this restriction, giving the power, is decided in *Child v. Hudson's Bay Company*, 2 P. Wms. 207. The agreement of the stockholders would be equally binding on them, and all who stand in their shoes, as a by-law. By-laws bind, because the members of the corporation, either individually, or by those who represent them, are supposed to give their assent to them. A course of dealing, a usage, an understanding, a contract express or implied, is the lien of the parties and a law to them, provided they are not repugnant to the charter or the laws of the land. This is contrary to neither. If the restrictive clause had been inserted in the Act of Incorporation, as it is in the charters of the Philadelphia Bank, Farmers' & Mechanics' Bank, and Union Bank of Georgetown, according to the decisions of the Supreme Court of the United States, in *The Union Bank v. Laird*, 'no person could acquire a real right to any share, except under a legal transfer, according to the rules of the bank, under the Act of Incorporation, of which he is bound to take notice.' The understood notice to Mr. Waln, his continuing to deal with the bank, with full knowledge of this term and condition, is equally binding on him, and the present plaintiffs, as if it were a written regulation, a by-law, a provision in the charter, or clause inserted in the very certificate of stock. The bank had an undoubted right to say to any stockholder, 'We discount your note; but remember, until it is paid, we shall hold your stock in security. You shall not be permitted to trans-

fer it until you pay us.' There is nothing unfair in this. The terms are known and are accepted as between the parties to the present agreement, the stockholder and the bank. This amounts to an hypothecation, a pledge of the stock. How it would have been in a controversy between a *bona fide* purchaser for valuable consideration and without notice, who pays his money to the stockholder on the faith of the certificate, intrusted with the symbol of the property, the constructive legal possession, the title-deed, on its face an instrument transferable and assignable, I do not give any opinion. It is a very different question." Cf. *Vansands v. Middlesex Co. Bank*, 26 Conn. 144 (1857). So in *Bryon v. Carter*, 22 La. Ann. 98 (1870), it is held that a by-law creating a lien, while it may be valid as between the parties, if it be brought to their knowledge, is not binding on the judgment-creditors of the shareholders.

² *Driscoll v. West Bradley, & Co., Co.*, 59 N. Y. 96, 109 (1874); *Bank of Holly Springs v. Pinson*, 58 Miss. 421 (1880); *Anglo-Californian Bank v. Grangers' Bank of California*, 63 Cal. 359. Cf. *Adley v. Whitstable Co.*, 17 Vesey, 316; *Slee v. Bloom*, 19 Johns. 456. A by-law of the New York Cotton Exchange provides that certificates of membership may be transferred only from member to member, but that no certificate shall be "so transferred until a notice of the intention to make such transfer, subscribed by the member owning the certificate, shall have been posted upon the bulletin of the exchange for ten days, and until all claims against such member which may be presented within said ten days by other members of the exchange, shall be settled, or while any annual dues or assessments levied on such membership shall remain unpaid." By-laws N. Y. Cotton Exchange, § 5. This by-law gives a lien upon the seat of every member in the exchange, not only to the exchange itself but to every other member thereof, to

although the transfer has not been recorded on the corporate books, cannot affect the rights of the parties as to that transfer. The by-law operates as a notice, and in order to be a notice, it must exist prior both to the transfer and the registry.¹ By-laws creating liens on stock have been, however, held valid and enforceable as against the assignees in bankruptcy or in insolvency.²

§ 525. *What phrases in charters or statutes will or will not authorize the corporation to create or enforce a lien on stock.*—The question sometimes arises whether or not the corporation has authority, reference being had to the language of the charter or the statute under which the corporation acts, to enact a by-law creating a lien upon its stock in favor of the corporation for debts due it by the shareholders. Accordingly there is found a line of cases which hold that, where the directors are authorized to make “regulations” as to transfers, they may make a by-law creating a lien.³ So also where shares are made, by statute, transferable “in such manner as the by-laws may direct,” as in the Louisiana Banking Act of 1855, it is held that a by-law may create a lien, provided that it does not, in effect, amount to a prohibition upon transfers.⁴ And where the charter of a bank made provisions for the transfer of stock “according to such rules as may, conformably to law, be established in that behalf by the president and directors,” a by-law, giving the bank a lien on the stock of any shareholder indebted to it, was sustained by the Supreme Court of the United States.⁵ It has also been held that a corporation organized under a statute which authorizes it to make by-laws for “the management of its property, the regulation of its affairs,” and “the transfer of its stock,”

secure the payment of any debt, the holder may owe either to the exchange or any member of it. In *People ex rel. Krohn v. Miller, Treas.*, 39 Hun, 557 (1886), Mr. Justice Daniels holds the by-law valid and enforceable, and considers at some length, in general, the validity and effect of such by-laws, regulating the sale and transfer of seats, or membership in the commercial exchanges, and the enforcement of the liens created thereupon by such by-laws in favor of other members of the corporation.

¹ *People v. Crockett*, 9 Cal. 112 (1858).

² *Morgan v. Bank of North America*,

8 Serg. & R. 73 (1822); s. c. 11 Am. Dec. 575; *Vansands v. Middlesex Co. Bank*, 26 Conn. 144 (1857). In *re Bigelow*, 1 Nat. Bank. Reg. 632 and 667 (1868).

³ *Cunningham v. Alabama, &c., Trust Co.*, 4 Ala. (N. S.) 652 (1843); *Spurlock v. Pacific R. R. Co.*, 61 Mo. 319 (1875); *Pendergast v. Bank of Stockton*, 2 Sawyer, 108 (1871). Cf. *Tuttle v. Walton*, 1 Ga. 43 (1846).

⁴ *Bryon v. Carter*, 22 La. Ann. 98 (1870).

⁵ *Brent v. Bank of Washington*, 10 Peters, 596, 611 *et seq.* (1836).

and further provides that the stock of the company "shall be transferable in such manner as shall be prescribed by the by-laws of the company," has the power to make a by-law providing that no transfer of stock shall be made upon the books of the corporation until after the payment of all indebtedness to the corporation, due from the person in whose name the stock stands on its books.¹ But in *Bullard v. Bank*,² it is held as to the national banks, that a by-law giving the bank a lien on the stock of the debtor, is not "a regulation of the business of the bank, or a regulation for the conduct of its affairs," within the proper meaning of those words in the National Banking Act of 1864, and, in consequence, not such a regulation as the national banks, under that act, have a right to make.³

§ 526. *The lien, when established, covers all the stockholder's shares and dividends.*—A valid lien in favor of the corporation, when regularly established, attaches in general to all the shares and dividends of the indebted stockholder. Thus, it attaches to all the shares the stockholder owns, although the debt be for calls due and unpaid upon only a part of them.⁴ In Virginia, however, it seems that there can be no lien on wholly paid up shares to secure the payment of an unpaid subscription to other shares.⁵ And in England, a lien on stock for unpaid calls is a lien only on those particular shares upon which the call is made, and not on other shares.⁶ The lien attaches not only to the stock itself, but to dividends declared on the stock,⁷ even though only

¹ *Pendergast v. Bank of Stockton*, 2 Sawyer, 108 (1871). Such a by-law, in order to be valid, must have been adopted by vote of a majority of the stockholders, and not merely by vote of the board of directors. *Carroll v. Mullanphy Savings Bank*, 8 Mo. App. 249; *Bank of Attica v. Manfg. Bank*, 20 N. Y. 501.

² 18 Wall. 589 (1873).

³ To the same effect, see *Delaware, &c., R. R. Co. v. Oxford Iron Co.*, 38 N. J. Eq. 340, and the notes; *Hagar v. Union National Bank*, 63 Me. 509 (1874); *Lee v. Citizens National Bank*, 2 Cin. 298, 306; *Evansville National Bank v. Metropolitan National Bank*, 2 Biss. 527 (1871). In the case last cited, which upon appeal was affirmed by the Supreme Court of the United States, it was held that such a by-law was in its operation the same thing as though a loan were

made by the bank upon the security of the stock—a transaction forbidden by the 35th section of the National Banking Act.

⁴ *Stebbins v. Phoenix Fire Ins. Co.*, 3 Paige, 350 (1832).

⁵ *Shenandoah Valley R. R. Co. v. Griffith*, 76 Va. 913 (1882). *Cf. Va. Code*, 1860, ch. 57, §§ 21, 22, 24; *Petersburg Savings, &c., Company v. Lumsden*, 75 Va. 327 (1881).

⁶ *Hubbersty v. Manchester, &c., Ry. Co.*, L. R., 2 Q. B. 471 (1867).

⁷ *Stebbins v. Phoenix Fire Ins. Co.*, 3 Paige, 350 (1832); *Bates v. New York Ins. Co.*, 3 Johns. Cas. 238 (1802); *Sargent v. Franklin Ins. Co.*, 8 Pick. 90 (1829); *Grant v. Mechanics Bank*, 15 Serg. & R. 140 (1826); *Hagar v. Union National Bank*, 63 Me. 509 (1874). In the case last cited it was held that even a

"shares and stock" be specifically named in the statute or charter as subject to the lien.¹ It is accordingly held that a corporation may lawfully retain dividends, and apply them to the payment of a debt due to it from the shareholder. And this is reasonable, since in an action by the shareholder to enforce payment of his dividends the corporation may always plead the debt by way of set-off.² But dividends declared after the death of the stockholder are not subject to a lien for his debts.³ The lien follows the proceeds of the shares after a liquidation or dissolution of the company.⁴ And attaches not only to valid stock, but to spurious stocks or shares obtained by forgery.⁵ So also the lien exists as to debts due from a trustee who holds stock in trust, but in his own name, and without any indication of the trust.⁶ And where a *cestui que trust* owes the corporation a debt the lien attaches to his stock though held for him in the name of a trustee.⁷

§ 527. *The lien protects the corporation as to all the debts due to it from the shareholder.*—It is a general rule that a lien upon shares of this nature is a lien as against all liabilities of the shareholder of every name and nature due to the corporation.⁸ And it is not material that the debt be due and payable at the time when the lien is sought to be enforced. It covers debts which are not due as well as those that are due, and all indebtedness to the corporation, whether payable presently or at a future time.⁹

national bank might have a lien on dividends, though it cannot have a lien on the stock itself. *Cf.* *Brent v. Bank of Washington*, 2 Cranch C. C. 517 (1824); *Klopp v. Lebanon Bank*, 46 Penn. St. 88 (1863).

¹ *Hague v. Dandeson*, 2 Exch. 147 (1848).

² *Hagar v. Union National Bank*, 63 Me. 509 (1874); *Sargent v. Franklin Ins. Co.*, 8 Pick. 90 (1829); *Bates v. New York Ins. Co.*, 3 Johns. Cas. 238 (1802). *Cf.* *Merchants Bank v. Shouse*, 102 Penn. St. 488; s. c. 16 Rep. 442; *Brent v. Bank of Washington*, 2 Cranch C. C. 517 (1824).

³ *Brent v. Bank of Washington*, 2 Cranch C. C. 517 (1824).

⁴ *In re General Exchange Bank*, L. R., 6 Chan. 818 (1871).

⁵ *Mt. Holly Paper Company's Appeal*, 99 Penn. St. 513 (1882).

⁶ *New London & Brazilian Bank v.*

Brocklebank, L. R., 21 Chan. Div. 302 (1882); *Young v. Vough*, 23 N. J. Eq. 325 (1873); *Burns v. Lawrie's Trustees*, 2 Scotch Ct. of Sessions Cas. (2d series), 1348 (1840), otherwise cited, 2 Dunlap, Bell & Murray, 1348.

⁷ *Stebbins v. Phoenix Fire Ins. Co.*, 3 Paige, 350 (1832).

⁸ *Union Bank of Georgetown v. Laird*, 2 Wheat. 390 (1817); *Mobile Mutual Ins. Co. v. McCallum*, 49 Ala. 558 (1873); *Cunningham v. Ala., &c. Trust Co.*, 4 Ala. (N. S.) 652 (1843); *Rogers v. Huntington Bank*, 12 Serg. & R. 77 (1824); *Ex parte Stringer*, L. R. 9 Q. B. Div. 436 (1882). *Cf.* *Hall v. United States Ins. Co.*, 5 Gill (Md.), 484 (1847); *In re Peebles*, 2 Hughes, 394 (1875); *Planters, &c. Mutual Ins. Co. v. Selma Savings Bank*, 63 Ala. 585 (1879).

⁹ *Pittsburgh, &c. R. R. Co. v. Clarke*, 29 Penn. St. 146 (1857); *In re Bachman*,

The lien also will survive to the advantage of the corporation, although the debt be barred by the Statute of Limitations.¹ The lien attaches whether the stockholder's debt to the corporation accrued before or after he became a stockholder. It also secures debts for which the shareholder is liable only as surety,² and debts due from a partnership in which the stockholder is a partner.³ So also it secures the corporation for unpaid calls upon the original subscription.⁴ And the call will be considered made at the

12 Nat. Bank. Reg. 223 (1875); *Downer's Admr. v. Zanesville Bank*, Wright (Ohio), 477 (1833); *Brent v. Bank of Washington*, 10 Peters, 596 (1836); *Grant v. Mechanics' Bank*, 15 Serg. & R. 140 (1826); *Rogers v. Huntington Bank*, 12 Id. 77 (1824); *Sewall v. Lancaster Bank*, 17 Id. 285 (1828); *McCready v. Rumsey*, 6 Duer, 574 (1857); *St. Louis Perpetual Insurance Co. v. Goodfellow*, 9 Mo. 149 (1845); *Cunningham v. Ala., &c. Trust Co.*, 4 Ala. (N. S.) 652 (1843); *Hall v. United States Ins. Co.*, 5 Gill (Md.), 484, (1847); *Leggett v. Bank of Sing Sing*, 24 N. Y. 283 (1862); *In re Stockton Malleable Iron Co.*, L. R. 2 Chan. Div. 101 (1875). In *Grant v. Mechanics' Bank*, 15 Serg. & R. 140 (1826), it was held that a bank organized under the Pennsylvania law of March 21, 1814, might lawfully refuse to permit the transfer of the stock of a shareholder who was the drawer of a bill discounted by the bank, but not payable at the time the transfer was demanded, both the shareholder and his indorser having, since the discount of the paper, become insolvent. *Acc. Downer's Admr. v. Zanesville Bank*, Wright (Ohio), 477 (1833). But where the lien is expressly made a security for debts "actually due and payable," it will be held to cover only debts due and payable. *Reese v. Bank of Commerce*, 14 Md. 271 (1859). *Cf. Downer's Admr. v. Zanesville Bank*, Wright (Ohio), 477 (1833).

¹ *Farmers' Bank of Maryland v. Iglehart*, 6 Gill (Md.), 50 (1847); *Geyer v. Western Ins. Co.*, 3 Pittsb. 41 (1867). *Cf. Brent v. Bank of Washington*, 10 Peters, 596 (1836).

² *Schmidt v. Hennepin County B. Co.*, 29 Northwest. Rep. 200 (Minn. 1886); *McLean v. LaFayette Bank*, 3 McLean, 587 (1846); *Leggett v. Bk. of Sing Sing*, 24 N. Y. 283 (1862); *Union Bk. of Georgetown v. Laird*, 2 Wheat. 390 (1817); *McDowell v. Bank of Wilmington & Brandywine*, 1 Harr. (Del.) 27 (1832); *Brent v. Bank*

of Washington, 10 Peters, 596 (1836); *St. Louis Perpetual Ins. Co. v. Goodfellow*, 9 Mo. 149 (1845). As to whether the lien extends to a guarantee of a certain income to the corporation, see *Miles v. New Zealand, &c. Co.*, 54 L. T. Rep. 582 (1886). It attaches to the stock of an indorser of a note upon a pretest. *West Branch Bank v. Armstrong*, 40 Penn. St. 278 (1861).

³ In the *Matter of Bigelow*, 2 Benedict, 469 (1868); *German Security Bank v. Jefferson*, 10 Bush, 326 (1874); *West Branch Bank v. Armstrong*, 40 Penn. St. 278 (1861); *Geyer v. Western Ins. Co.*, 3 Pittsb. 41 (1867); *Arnold v. Suffolk Bank*, 27 Barb. 424 (1857); *Planters, &c. Ins. Co. v. Selma Savings Bank*, 63 Ala. 585 (1879).

⁴ *Morgan v. Bank of North America*, 8 Serg. & R. 73 (1822); s. o. 11 Am. Dec. 576; *Spurlock v. Pacific R. R. Co.*, 61 Mo. 319 (1875); *McCready v. Rumsey*, 6 Duer, 574 (1857); *Regina v. Wing*, 33 Eng. L. & E. 80 (1855); *Ex parte Littledale*, L. R. 9 Chan. 257 (1874); *Companies Clauses Consolidation Act*, 1845 (8 Vict. chap. 16, § 16). *Contra, Hall v. United States Ins. Co.*, 5 Gill (Md.), 484 (1847). In *Pittsburgh, &c. R. R. Co. v. Clarke*, 29 Penn. St. 146 (1857), it is held that the liability of the stockholder to pay for his stock is an indebtedness to the corporation within the meaning of that section of the General R. R. Act, which provides that no transfer can be made by a person indebted to the company. And in *Rogers v. Huntington Bank*, 12 Serg. & R. 77 (1824), it was held that a bank, organized in Pennsylvania under the act regulating banks of that State, passed March 21, 1813 (6 Sm. L. 154), which act provided that "no stockholder indebted to the institution shall be authorized to make a transfer or receive a dividend, till such debt shall have been discharged, or security, to the satisfaction of the directors, given for the same," had a lien on the

time when the shareholder is regularly notified of the resolution of the board of directors making the call. The company cannot be required to accept a transfer until every such call has been paid.¹ Whether the lien will avail to protect the corporation as to instalments on the stock not called, seems not to be settled. In Maryland,² and Missouri,³ it is held that it will not, while in some other jurisdictions there is a contrary rule.⁴ After a shareholder has regularly notified the corporation that he has transferred his stock, the corporation cannot avail itself of a lien on that stock to secure debts of the transferrer contracted subsequently to the transfer.⁵ But where the shareholder transfers his stock, and subsequently, without notifying the corporation of the transfer, borrows money from the corporation in the regular course of business, the corporation may refuse to register the transfer and insist upon the lien.⁶ The lien also attaches to the stock of a depositor who has overdrawn his account.⁷ And the corporation, in discounting a bill or note, may take security from one of the parties, and also hold the shares of another party as security for the same loan.⁸ If the shareholder's indebtedness to the bank is

stock of any shareholder who was in arrears to the bank, either upon his subscription to the capital stock, or on a note discounted in the regular order of business.

In Virginia the statutory lien on shares conferred by the provision of the Code (Code of 1860, chap. 57, §§ 21, 22, 24), is a lien *only* for the unpaid balance of the subscription price. *Petersburg Savings, &c. Co. v. Lumsden*, 75 Va. 327 (1881).

¹ *Shaw v. Rowley*, 5 Eng. Ry. & Canal Cas. 47 (1847); *Ex parte Tooke*, 6 Id. 1 (1849). *Cf. Newry, &c. Ry. Co. v. Edmunds*, 2 Exch. 118 (1848); *Ambergate, &c., Ry. Co. v. Mitchell*, 4 Id. 540 (1849); *Great North of England Ry. Co. v. Bidulph*, 7 Mees. & W. 243 (1840); *Regina v. Wing*, 33 Eng. L. & E. 80 (1855).

² *Hall v. United States Ins. Co.*, 5 Gill (Md.), 484 (1847).

³ *Kahn v. Bank of St. Joseph*, 70 Mo. 262 (1879). In this case it is held that where the lien is created to protect the corporation as to "arrears" and "indebtedness" to the corporation, it is not to be extended to uncalled instalments of subscription.

⁴ *In re Bachman*, 12 Nat. Bank. Reg. 223 (1875). In this case it is said that the construction put upon a by-law creat-

ing a lien on stock, by the corporate officers, will not bind the court in construing it.

⁵ *Conant v. Seneca County Bank*, 1 Ohio St. 298 (1853). But see *Union Bank of Georgetown v. Laird*, 2 Wheat. 390 (1817).

⁶ *Platt v. Birmingham Axle Co.*, 41 Conn. 255 (1874).

⁷ In *Reese v. Bank of Commerce*, 14 Md. 271 (1859), where the charter of the bank provided that "all debts actually due and payable to the corporation by a stockholder requesting a transfer, must be satisfied before such transfer shall be made, unless the president and directors shall direct to the contrary," it was held that this creates a lien in favor of the bank which attaches to balances due the bank by the stockholder, for overdrafts on checks, but not to notes and bills on which the shareholder may be a party, or maker, or indorser, which are not due at the time the transfer is demanded.

⁸ *Union Bank of Georgetown v. Laird*, 2 Wheat. 390 (1817); *First National Bank of Hartford v. Hartford, &c. Insurance Co.*, 45 Conn. 22 (1877). *Cf. Conant v. Seneca County Bank*, 1 Ohio St. 298 (1853); *Helm v. Swiggett*, 12 Ind. 194

less than the value of his stock, the bank, if it has a lien on the stock, may hold the whole until the debt is paid. They are not obliged to appropriate part of the stock to the payment of the debt and transfer the rest.¹ But there can be no lien as to debts created before the right of lien was granted.² In *Bishop v. Globe Company*,³ the rule is declared that if, by the law of the State under which a corporation is organized, the corporation has a lien on the stock of any shareholder for a debt due from him to the corporation, that lien is a good defense to an action in another State against the corporation by a person to whom the shareholder has transferred his stock, but in whose name, by reason of the lien, the corporation has refused to register the transfer. Where the corporation claims a lien when it is not entitled thereto, the transferee may hold it liable in damages.⁴

§ 528. *No lien for the debts of an unrecorded transferee.*—

The lien of a corporation on shares of stock as security for the payment of debts due to the corporation from the owner, is a lien only as to the indebtedness of duly recorded shareholders. There is, in general, no lien on the stock as to debts of an intervening unrecorded owner of the stock.⁵ But there may be a contrary sale in equity where the lien is created by a by-law.⁶ And if the charter or an authorized by-law provides that no transfer or assignment of stock shall be valid unless made on the books of the company, an individual obtaining an assignment of shares from an apparent owner, which assignment is not registered on the books of the company, takes it subject to all the equitable rights

(1859). But where one borrowed money from a bank upon his title deeds as security, it was held, upon his death, the question arising, upon the settlement of the estate, as to what part of the estate should be charged with payment of certain debts, that his shares of stock in the bank need not contribute ratably with the real estate toward the repayment of the sum borrowed from the bank, merely because the deed of settlement of the bank gave it a lien on its shares for debts due to it by the shareholder, for the reason, as it seems, that the loan having been made upon the security of the real estate, and the security being ample, there was no reason that the bank should assert its lien on the stock except to favor one class

of the beneficiaries of the decedent over another class, something the bank was not called upon to do. *Dunlop v. Dunlop*, L. R. 21 Chan. Div. 583 (1882).

¹ *Sewall v. Lancaster Bank*, 17 Serg. & R. 285 (1828); *Acc. Pierson v. Bank of Washington*, 3 Cranch C. C. 363 (1828).

² *People v. Crockett*, 9 Cal. 112 (1858).
³ 135 Mass. 132 (1883).

⁴ *Skinner v. City of London, & Co.*, 53 L. T. 191 (1885), holding also that the measure of damages is not the secret price of the stock transferred.

⁵ *Helm v. Swiggett*, 12 Ind. 194 (1859).

⁶ *Planters, & Co. Ins. Co. v. Selma Savings Bank*, 63 Ala. 585 (1879).

of the company against the real owner thereof.¹ A pledgee who is duly registered on the corporate books as a shareholder, but to whom no certificate has been issued, is nevertheless protected against liens upon his shares for the indebtedness of the pledgor.² But a pledgee who neglects to notify the corporation that he holds the stock in pledge, or to take the proper steps to secure title to the stock in his own name, will not be protected against the lien of the corporation upon the stock to secure the payment of an indebtedness contracted to the bank by the pledgor in the meantime, and subsequently to the pledge of the shares.³ Stock standing on the corporate books in the name of a fictitious person is subject to a lien for the indebtedness of the real owner.⁴ A corporate lien for the debts of a legatee will not attach to stock unless the legatee accept the shares.⁵

§ 529. *The lien can be enforced for the benefit of the corporation only.*—The right of a corporation to a lien on the stock of its shareholders as security for the payment of their debts to the corporation, is a right to be enforced only by the corporation and exclusively for its own benefit. Accordingly it is held that the corporation cannot become the assignee of the claim of some third person against one of its shareholders in order to enforce payment of that claim for the benefit of the third person by a recourse to the corporate lien on the shareholder's stock.⁶ Neither can the corporation be compelled, for the benefit of sureties as to a part of the shareholder's indebtedness, to apply the proceeds of the sale of the stock to the liquidation of that part of their claim which is secured. The lien is for the benefit of the corporation, and it may apply the proceeds of the sale of the stock in such a way as best to subserve its own interest.⁷ There seems to be a contrary rule in Delaware,⁸ Virginia,⁹ and Pennsylvania,¹⁰ but, as the author believes, not well grounded. But where one pays a

¹ Stebbins v. Phoenix Fire Ins. Co. 3 Paige, 350 (1832).

² National Bank v. Watsontown Bank, 105 U. S. 207 (1881).

³ Platt v. Birmingham Axle Co., 41 Conn. 255, 264 (1874).

⁴ Stebbins v. Phoenix Fire Ins. Co., 3 Paige, 350 (1832).

⁵ Farmers Bank of Maryland v. Iglehart, 6 Gill (Md.), 50 (1847).

⁶ White's Bank v. Toledo, &c. Ins. Co., 12 Ohio St. 601 (1861). To the point

that this lien is one exclusively for the benefit of the corporation see Bank of Utica v. Smalley, 2 Cowen, 770 (1824).

⁷ Cross v. Phenix Bank, 1 R. I. 39 (1840).

⁸ Hardcastle v. Commercial Bank, 1 Harr. 374 n. (1831).

⁹ Petersburg Savings, &c. Co. v. Lumsden, 75 Va. 327 (1881).

¹⁰ Kubns v. Westmoreland Bank, 2 Watts (Penn.), 136 (1833); Klopp v. Lebanon Bank, 46 Penn. St. 88 (1863).

debt as surety for a shareholder, he is entitled to be subrogated to the rights of the corporation by way of lien on the shareholder's stock.¹ And where the transferee pays the transferor's debt to the corporation, in order to obtain a registry of the transfer, he may have his action to recover back the amount so paid from his transferor.²

§ 530. *Methods of enforcing the lien.*—When a corporation has a lien upon the stock of those of its shareholders who are indebted to it, it may refuse to allow a transfer of the stock until the debt is paid or secured to its satisfaction. This is the usual method of enforcing the lien.³ And the corporation may insist upon its lien and hold the stock even against a *bona fide* purchaser at an execution sale.⁴ It may, moreover, hold the whole amount of the shareholder's stock, although the amount of the debt be less than the value of the shares. It cannot be compelled to transfer so much of the stock as is in excess of the amount of the debt.⁵ The corporation can enforce its lien against the transferee only by a refusal to allow the transfer. It cannot elect to make the transferee personally liable for the debt, but as against the transferor the corporation may proceed by an attachment of the stock.⁶ So, also, upon non-payment of the debt, the corporation may make an application to a court of chancery and have the shares sold in the usual way, as in other cases of property held under a lien.⁷ A

¹ *Young v. Vough*, 23 N. J. Eq. 325 (1873); *Hodges v. Planters Bank*, 7 Gill & J. 306, 310 (1835); *West Branch Bank v. Armstrong*, 40 Penn. St. 278 (1861); *Klopp v. Lebanon Bank*, 46 Id. 88 (1863); *Hardcastle v. Commercial Bank*, 1 Harr. (Del.) 374 n. (1831). Cf. *Higgs v. Assam Tea Co.*, L. R. 4 Exch. 387 (1869); *In re Northern Assam Tea Co.*, L. R. 10 Eq. 458 (1870); *National Exchange Bank v. Silliman*, 65 N. Y. 475 (1875).

² *Bates v. New York Ins. Co.*, 3 Johns. Cas. 238 (1802).

³ *Reese v. Bank of Commerce*, 14 Md. 271 (1859); *Brent v. Bank of Washington*, 10 Peters, 596 (1836); *First National Bank of Hartford v. Hartford, &c. Ins. Co.*, 45 Conn. 22 (1877); *Vansands v. Middlesex County Bank*, 26 Conn. 144 (1857); *Farmers Bank of Maryland v. Iglehart*, 6 Gill (Md.), 50 (1847); *McCready v. Rumsey*, 6 Duer, 574 (1857); *Tuttle v. Walton*, 1 Ga. 43 (1846); *Sewall v. Lancaster Bank*, 17 Serg. & R. 285

(1828); *Rogers v. Huntington Bank*, 12 Id. 77 (1824); *Grant v. Mechanics Bank*, 15 Id. 140 (1826). Cf. *Sabin v. Bank of Woodstock*, 21 Vt. 353 (1849); *West Branch Bank v. Armstrong*, 40 Penn. St. 278 (1861).

⁴ *Newbury v. Detroit, &c. R. R. Co.*, 17 Mich. 141 (1868); *Titcomb v. Union, &c. Ins. Co.*, 8 Mass. 326 (1811); *Rogers v. Huntington Bank*, 12 Serg. & R. 77 (1824); *Grant v. Mechanics Bank*, 15 Id. 140 (1826); *Sewall v. Lancaster Bank*, 17 Id. 285 (1828); *West Branch Bank v. Armstrong*, 40 Penn. St. 278 (1861); *Mechanics Bank v. Merchants Bank*, 45 Mo. 513 (1870); *St. Louis Perpetual Life Ins. Co. v. Goodfellow*, 9 Id. 149 (1845); *Tuttle v. Walton*, 1 Ga. 43 (1846).

⁵ *Sewall v. Lancaster Bank*, 17 Serg. & R. 285 (1828); *Pierson v. Bank of Washington*, 3 Cranch C. C. 363 (1828).

⁶ *Sabin v. Bank of Woodstock*, 21 Vt. 353 (1849).

⁷ *In re Morrison*, 10 Nat. Bank. Reg.

decree authorizing the sale of the stock for the payment of the debt need not give the shareholder the right of redemption. An absolute and valid title may pass to the purchaser immediately upon the sale.¹ A valid lien in favor of a bank upon shares of stock in the bank belonging to the estate of a deceased person, will not yield to a prior claim against the estate in favor of the government.² But an unwarranted claim of lien by a corporation, and a consequent refusal to register a transfer, until the debt as to which the lien is asserted is paid, is a conversion of the shares, and the transferrer may have his action against the corporation therefor.³ In order, however, to put the corporation in the wrong, for a refusal to transfer, where it claims more than is due, the shareholder must tender what he admits to be due.⁴

§ 531. *The corporation may waive its lien.*—A corporation is no more bound to collect a debt for which it holds a lien upon shares of its own stock, than any other pledgee or mortgagee is to enforce or foreclose his lien. The lien may be asserted and enforced, or in the discretion of the corporation it may be waived.⁵

105 (1874); *Farmers Bank of Maryland's Case*, 2 Bland's Chan. (Md.) 394 (1830); *Brent v. Bank of Washington*, 10 Peters, 596 (1836).

¹ *Reese v. Bank of Commerce*, 14 Md. 271 (1859). In one case the lien was held to be equivalent to a pledge, and it was held that after giving due notice to the delinquent shareholder the corporation might sell at public auction, without filing a bill to foreclose. *Farmers Bank of Maryland's Case*, *supra*. In this case it is held that where the corporation neglects or refuses to sell the stock of a deceased shareholder, who is in arrears, the administrator may file a bill and obtain an order of sale directed to the corporation.

² *Brent v. Bank of Washington*, 10 Peters, 596 (1836).

³ *Bank of America v. McNeil*, 10 Bush, 54 (1873). *Cf. Dickinson v. Central National Bank*, 129 Mass. 279 (1880). See *Case v. Bank*, 100 U. S. 446 (1879).

⁴ *Pierson v. Bank of Washington*, 3 Cranch C. C. 363, (1828). In *German Security Bank v. Jefferson* (10 Bush, 326, 1874), it was held that where the stock sold under the lien realized a sum insufficient to satisfy the corporate debt, the unpaid balance of the claim of the corporation could not be paid until there had

been a proportionate payment of the claims of other creditors of the shareholder out of his general assets, as in the distribution of assets, in general, in the case of an insolvent partnership. In this case the shareholder being largely indebted to the bank, became insolvent and made an assignment for the benefit of his creditors. The sale of his bank stock did not pay in full what he owed the bank. The bank thereupon claimed the right to come in equally with other creditors in the distribution of the general assets, but the court held that the other creditors must first be paid proportionally as much as the bank had secured by reason of its lien. "And," says the court, per Lindsay, J., "when this is done the balance will then be distributed *pari passu* among all the creditors." *German Security Bank v. Jefferson*, 10 Bush, 326 (1874). *Cf. Northern Bank of Kentucky v. Keizer*, 2 Duv. 169; *In re Peebles*, 2 Hughes, 394 (1875).

⁵ *National Bank v. Watsonstown Bank*, 105 U. S. 217 (1881); *s. c. sub nom. Cecil National Bank v. Watsonstown Bank*, 21 Am. Law Reg. (N. S.) 545; *Hodges v. Planters Bank*, 7 Gill & J. 306 (1835); *Chambersburg Ins. Co. v. Smith*, 11 Penn. St. 120 (1849); *Hall v. United States Ins. Co.*, 5 Gill (Md.), 484 (1847); *In re Hoy*

Cases may arise where the intervening rights of other creditors of the shareholder render it inequitable for the corporation to waive its lien on the stock,¹ but in general, the right of the corporation at its option to waive the lien is absolute.

Accordingly, where a note discounted for a shareholder, was protested for non-payment, it was held that the bank might waive its lien on the stockholder's shares in the bank, and proceed directly against the indorser.² And the corporation, by waiving the lien, does not discharge a surety unless the surety has given the corporation express notice not to waive the lien.³ The corporation will not be held to have waived its lien upon the stock of its debtor, merely because it has taken other, or additional, security for the debts;⁴ nor because it assents to a general assignment by the shareholder for the benefit of creditors.⁵ And the corporation may allow the transfer of a portion of a shareholder's stock without waiving its lien on the rest.⁶ But a waiver of the lien for a limited time is fatal, provided the stock is transferred during that time.⁷

A waiver which will bind the corporation may, in the absence of some thing to qualify the power, be made by the cashier of a bank, acting by virtue of an express or implied authority, for the board of directors,⁸ or the secretary of an insurance company,⁹ or the general manager or properly qualified general agent of the

lake Ry. Co., L. R., 9 Chan. 257, 259 (1874). But see *Conant v. Seneca Co. Bank*, 1 Ohio St. 298, 301 (1853). A lien does not proceed of its own vitality, but the officers of the corporation must set it in motion or they gain nothing by it. It is merely a reserved right in favor of the corporation, and it is effectual to protect the corporation only when it elects to avail itself of it, in the prescribed manner. If the corporation take no steps to enforce its lien, the owner not being divested of his title, some other creditor may step in and may reach the value of the stock in excess of the amount of the lien. *In re Bigelow*, 1 Nat. Bank. Reg. 667 (1868). A waiver is the intentional relinquishment of a known right. It is not to be inferred, and imputed to a corporation, in the absence of proof of it, and a mere failure to assert the lien is not equivalent to a relinquishment or waiver of it. *First National Bank of Hartford v. Hartford, &c., Ins. Co.*, 45 Conn. 22, 43 (1877).

¹ *In re Bachman*, 12 Nat. Bank. Reg. 223 (1875).

² *Cross v. Phenix Bank*, 1 R. I. 39 (1840).

³ *Perrine v. Fireman's Ins. Co.*, 22 Ala. 575 (1853).

⁴ *Union Bank of Georgetown v. Laird*, 2 Wheat. 390 (1817).

⁵ *Dobbins v. Walton*, 37 Ga. 614 (1868).

⁶ *First National Bank of Hartford v. Hartford, &c., Insurance Co.*, 45 Conn. 22 (1877). But see *contra*, *Presbyterian Congregation v. Carlisle Bank*, 5 Penn. St. 345 (1847).

⁷ *Bank of America v. McNeil*, 10 Bush, 54 (1873).

⁸ *National Bank v. Watsontown Bank*, 105 U. S. 217 (1881). So also the refusal of the cashier to permit a transfer is the act of the bank for which it may be charged. *Case v. Bank*, 100 U. S. 446 (1879).

⁹ *Chambersburg Ins. Co. v. Smith*, 11 Penn. St. 120 (1849).

corporation, especially if that is a general custom of the company.¹ Accordingly, where one buys shares on the faith of a representation of the corporate officers, that the stock is unincumbered, he is entitled to the shares free from any corporate lien.²

And where the corporate officers allow a transfer to be registered, and a new certificate to be issued, there is a waiver of the corporate lien as to the debts of the transferrer.³ So also a by-law, requiring the consent of the board of directors to a transfer by one indebted to the corporation, is held to be repealed, where a custom of disregarding it has been shown, it appearing also that the secretary had been allowed to exercise his own discretion about such transfers, without consulting the directors. In such a case, the consent of the secretary to the transfer is a waiver of the lien.⁴

It is held that a failure to recite the lien, on the face of the certificate, is not a waiver of the lien,⁵ and that a statement in the certificate, that the holder is entitled to a certain number of shares, transferable upon presentation and surrender thereof, in the absence of any assertion of a lien, is not a waiver of the lien, but a mere indication of the manner in which the shares are to be transferred.⁶ When the lien is given to the corporation by the charter, or the articles of association, or by statute, there is constructive notice to all persons dealing with the corporation, that they must, at their peril, without reference to what the certificate recites or fails to recite, inform themselves as to any incumbrance that may affect the shares they propose to buy. If there is a lien they are held to have known it, whether the certificate declares it or not.

But where the lien is created by a by-law, it is something of which purchasers of the shares cannot so strictly be held to have had constructive notice. In such a case, if the certificate does not disclose the lien, and actual knowledge of it be not shown, a *bona*

¹ See *Bishop v. Globe Company*, 135 Mass. 132 (1888); *Young v. Vough*, 23 N. J. Eq. 325 (1873).

² *Moore v. Bank of Commerce*, 52 Mo. 377 (1873).

³ *Hill v. Paine River Bank*, 45 N. H. 300 (1864); *Higgs v. Assam Tea Co.*, L. R., 4 Exch. 387 (1869). *In re Northern Assam Tea Co.*, L. R., 10 Eq. 458 (1870).

⁴ *Chambersburg Ins. Co. v. Smith*, 11 Penn. St. 120 (1849).

⁵ *Reese v. Bank of Commerce*, 14 Md. 271 (1859); *McCready v. Rumsey*, 6 Duer, 574 (1857). In *Hoffman Steam Coal Co. v. Cumberland Coal & Iron Co.*, 16 Md. 456 (1860), it is held that a lien avails, though it be not recited on the face of the certificate, against even a *bona fide* purchaser.

⁶ *First National Bank of Hartford v. Hartford, &c., Ins. Co.*, 45 Conn. 22, and the cases cited in the preceding note.

fide purchaser would be protected. Recitals in the certificate as to a lien are, therefore, material only when the lien has been created by a by-law. In that case, there must be actual notice of the lien, or the corporation is not protected. But when the lien is part of the constitution of the corporation, that is when it is created by statute or the charter of the corporation, there is constructive notice, and the corporation is protected without reference to the recitals of the certificates of stock.¹

§ 532. *The lien as affected by transfers and notice.*—Upon a transfer, as between transferrer and transferee, title to the stock passes absolutely, although the corporation, in the assertion of a lien upon the stock for the indebtedness of the transferee, refuses to register the transfer until the debt is paid or otherwise secured.² But, of course, the assignee or transferee, or whoever succeeds to the rights of the shareholder in the stock, takes it subject to the lien of the corporation.³ And when the stock is sold by the corporation to pay the debts of the transferrer, the transferee is entitled to the surplus, if any there be, which remains after the claim of the corporation is satisfied.⁴

The corporation cannot, after it has been regularly notified of the transfer, assert a lien upon the stock to secure an indebtedness of the transferrer contracted subsequently to the notice.⁵ A mere notice to the bank is, in such a case, sufficient to protect the transferee. It is immaterial that the transfer was not regis-

¹ Bank of Holly Springs v. Pinson, 58 Miss. 421 (1880); Fitzhugh v. Bank of Shepherdsville, 3 Mon. (Ky.) 126 (1825); Anglo-Californian Bank v. Grangers' Bank of California, 63 Cal. 359. See § 523.

² National Bank v. Watson town Bank, 105 U. S. 217 (1881); Johnson v. Laffin, 103 Id. 800 (1880); Duke v. Cahawba Navigation Co., 10 Ala. 82 (1846); St. Louis Perpetual Life Ins. Co. v. Goodfellow, 9 Mo. 149 (1845); Commercial Bank of Buffalo v. Kortright, 22 Wend. 348 (1839); s. c. *sub nom.* Kortright v. Buffalo Commercial Bank, 20 Id. 91 (1838); Bank of Utica v. Smalley, 2 Cowen, 770 (1824); McNeil v. Tenth National Bank, 46 N. Y. 325 (1871); People *ex rel.* Krohn v. Miller, 39 Hun, 557, 563 (1886). Cf. Dunn v. Commercial Bank of Buffalo, 11 Barb. 580; Davis v. Bechstein, 69 N. Y. 440 (1877); Merchants Bank v. Livingston,

74 Id. 223 (1878); Pittsburgh, &c., R. R. Co. v. Clarke, 29 Penn. St. 146 (1857); Sargent v. Essex Marine Ry. Corp. 9 Pick. 202 (1829); Carroll v. Mullanphy Savings Bank, 8 Mo. App. 249 (1880).

³ Mobile Mutual Ins. Co. v. Cullom, 49 Ala. 558 (1873); New Orleans National Banking Association v. Wiltz, 4 Woods, 43 (1881); s. c. 10 Fed. Rep. 330.

⁴ Weston v. Bear River, &c., Mining Co., 5 Cal. 186 (1855); Tuttle v. Walton, 1 Ga. 43 (1846); Foster v. Potter, 37 Mo. 325 (1866); West Branch Bank v. Armstrong, 40 Penn. St. 278 (1861).

⁵ Conant v. Seneca County Bank, 1 Ohio St. 293 (1853); Nesmith v. Washington Bank, 6 Pick. 324 (1828). Cf. Platt v. Birmingham Axle Co., 41 Conn. 255 (1874); Union Bank of Georgetown v. Laird, 2 Wheat. 390 (1817).

tered.¹ And in a case where the transfer was registered but no certificate had been issued, it was held that a pledgee was protected.² But where there is neither a register of the transfer, nor notice of it served upon the corporation, the stock may properly be subjected to a corporate lien for the indebtedness of the transferrer, incurred subsequently to the transfer.³ In *Pitot v. Johnson*,⁴ it is held that a corporate lien, for the debts of the transferrer, contracted after the transfer, will not attach to the stock, even though no notice of the transfer has been given to the corporation.⁵ In England, the rule has recently been settled that a provision in the articles of association creating a paramount lien on shares in favor of the corporation, gives the company priority over a mortgagee of the shares, or over one whose claim is an equitable one, of whose charge upon the shares the company had notice before the specific liability of the shareholder toward the company has been incurred.⁶

§ 533. *Liens on national bank stock.*—National banks were formerly held to have power to enact by-laws creating a lien on stock in the bank for debts owed by its owner to the bank.⁷ But

¹ *Bank of America v. McNeil*, 10 Bush, 54 (1873).

² *Cecil National Bank v. Watson*, 21 Am. Law Reg. (N. S.) 545 (1881); s. c. *sub nom.* *National Bank v. Watson*, 105 U. S. 217.

³ *Platt v. Birmingham Axle Co.*, 41 Conn. 255 (1874).

⁴ 33 La. Ann. 1286 (1881).

⁵ Upon the question of notice as affecting the right of a member of the New York Cotton Exchange to transfer his membership, see *People ex rel. Krohn v. Miller*, 39 Hun, 557 (1886), and a full discussion of the matter of notice by Mr. Justice Daniels.

⁶ The case in which this rule is, after much contest, explicitly declared, is *Bradford Banking Co. v. Briggs*, L. R., 31 Chan. Div. 19 (1885); s. c. 53 L. T. Rep. (N. S.) 846; reversing s. c. L. R., 29 Chan. Div. 149 (1885). See also *Miles v. New Zealand Alford Estate Company*, 54 L. J. Chan. 1035 (1885); s. c. Week. Notes (1885), page 142; s. c. 53 L. T. Rep. (N. S.) 219; *Re Dunlop*, 48 L. T. Rep. (N. S.) 89 (1883); *Societe Generale De Paris v. Tramways Union Company*, L. R., 14 Q. B. Div. 424; *Hopkinson v. Rolt*, L. R., 9 H. L. Cas. 514; *New Lon-*

don & Brazilian Bank v. Brocklebank, L. R. 21 Chan. Div. 302 (1882), where it appears that the articles of association of a company, registered under the Companies Act of 1862, gave the company a first lien on every share for all debts due from the shareholder to the company. A shareholder deposited his certificate with his bankers, as security for a balance due the bank on his current account, and notice of the deposit was given to the company. The certificate stated that the shares were held subject to the articles of association. It was held that the company might claim priority over the bankers in respect of moneys which became due from the shareholder to the company, even after notice of the bankers' advances had been given, because the company's lien was a first lien as against all persons claiming only equitable interests, and having notice of the articles of association, and because by the deposit of the certificate, the bankers acquired only an equitable interest, or that only a trust was created in their favor, and that the Companies Act of 1862, § 30, relieved the company from taking notice of any mere trust, created in respect of its shares.

⁷ The leading case was *Knight v. The*

the Supreme Court of the United States, when the question came before it, refused to enforce such a by-law, and decided that its enactment was not within the spirit of those provisions of the National Banking Act of 1864, which confer power upon the management of a national bank to regulate the business of the bank, and to conduct its affairs.¹ In the present state of the law, therefore, no national bank can, by any by-law, create any lien upon shares of stock in the bank to secure the payment of any indebtedness which the owner of the shares may contract to the bank.²

Old National Bank, 3 Clifford, 429 (1871), wherein Mr. Justice Clifford sustained such a by-law with much cogency of reasoning. In this case it was declared that the directors of a national bank may lawfully enact and enforce a by-law to the effect that "no person indebted to the bank shall be allowed to sell or transfer his or her stock without the consent of a majority of the directors, and this whether liable as principal or surety, and whether the debt or liability is due or not." To the same effect see *Lockwood v. Mechanics National Bank*, 9 R. I. 308 (1869); *In re Dunkerson*, 4 Biss. 227 (1868); *Young v. Vough*, 23 N. J. Eq. 235 (1873).

¹ *Bullard v. Bank*, 18 Wall. 589 (1873). See also *Bank v. Lanier*, 11 Id. 369 (1870); *Case v. Bank*, 100 U. S. 446 (1879).

² *Delaware, &c., R. R. Co. v. Oxford Iron Co.*, 38 N. J. Eq. 340 (1884); *Myers v. Valley National Bank*, 18 Nat. Bank. Reg. 34 (1878); *Hagar v. Union National Bank*, 63 Me. 511 (1874); *New Orleans National Bank v. Wiltz*, 10 Fed. Rep. 330 (1881); *s. c.* 4 Woods, 43; *Second National Bank of Louisville v. National State Bank of New Jersey*, 10 Bush, 367 (1874); *Evansville National Bank v. Metropolitan National Bank*, 2 Biss. 527 (1871). *Cf.* *National Bank of Xenia v. Stewart*, 107 U. S. 676 (1882); *Rosenbach v. Salt Springs National Bank*, 53 Barb. 495 (1868). This accords with the more general rule in New York, which holds all such by-laws of any corporation in that State invalid. See § 522.

CHAPTER XXXII.

DIVIDENDS ON STOCK.

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| <p>§ 534. Definition of a dividend, and the relation of shareholders thereto.</p> <p>535. Four kinds of dividends.</p> <p>536. Scrip dividends and property dividends.</p> <p>537. Stock dividends.</p> <p>538. Interest-bearing stock.</p> <p>539-40. Dividends can be made only from net profits.—Net profits defined.</p> <p>541. Discretion of the directors as to declaring dividends.</p> <p>542. To whom the dividend is to be paid.</p> <p>543. To whom the dividend belongs.</p> <p>544. Dividends must be equal and without preferences.</p> | <p>§ 545. Dividend when declared is a debt due absolutely to the shareholder.</p> <p>546. It is a debt which may be collected by legal proceedings.</p> <p>547. Right of the corporation to apply dividends to the payment of debts due to it by the shareholder.</p> <p>548. Dividends which impair the capital stock are illegal, and may be recovered back from the stockholders.</p> <p>549. Proceedings to recover back such a dividend.</p> <p>550. The liability herein of the corporate officers.</p> |
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§ 534. *Definition of a dividend, and the relation of shareholders thereto.*—A dividend is a corporate profit set aside, declared, and ordered by the proper corporate authorities, to be paid to the stockholders on demand or at a fixed time.¹ A dividend becomes the property of the shareholder, and the shareholder acquires his legal right thereto, only when it is regularly declared.² Inasmuch as a dividend can be declared only out of

¹ Lockhardt v. Van Alstyne, 31 Mich. 76 (1875); Webb v. Earle, L. R., 20 Eq. 556 (1875); Chaffee v. Rutland R. R. Co., 55 Vt. 110 (1882).

² Hyatt v. Allen, 56 N. Y. 553 (1874); Jones v. Terre Haute, &c., R. R. Co., 57 Id. 196 (1874); Brundage v. Brundage, 1 Thomp. & C. 82 (1873); aff'd, 60 N. Y. 544 (1875); Lockhardt v. Van Alstyne, 31 Mich. 76, 78 (1875); Gordon's Executors v. Richmond, &c., R. R. Co., 78 Va. 501 (1884); Dalton v. Midland Counties Ry. Co., 13 C. B. 474 (1853). Cf. Curry v. Woodward, 44 Ala. 305 (1870). In Faucett v. Lourie, 1 Drew. & Sm. 192 (1860), it was held that a declaration of a dividend gives the shareholders such a legal right to the payment of it, that a court of chancery will not, at the suit of

a single shareholder, interfere by an injunction to restrain the directors from paying it, while at the same time, in such a suit, it will in a proper case grant an injunction as to future and undeclared dividends. Cf. Stevens v. South Devon Ry. Co., 9 Hare, 313 (1851). Surplus profits before a dividend is declared belong to the corporation, and not to the shareholders. Until, therefore, a dividend is regularly declared, surplus profits are liable for corporate indebtedness. Curry v. Woodward, 44 Ala. 305 (1870); Goodwin v. Hardy, 57 Me. 143, 145 (1869); Rand v. Hubbell, 115 Mass. 461, 474 (1874). Suits against corporations to enforce the payment of dividends cannot be maintained until a demand has been made and payment refused. State

net profits which may or may not be earned, a shareholder, it is clear, is not absolutely but only contingently entitled to a dividend, and he is, therefore, in no proper sense, in respect thereto, a creditor of the corporation until the dividend is declared and made absolutely payable.¹

§ 535. *Four kinds of dividends.*—A corporation may, in general, make four different kinds of dividends; namely, a dividend payable in cash, in certificates of stock, in scrip, or in property. In the absence of a special provision to the contrary, dividends will be presumed to be payable in cash, and in lawful or current money.²

§ 536. *Scrip dividends and property dividends.*—A scrip dividend is a dividend of certificates giving the holder certain rights which are specified in the certificate itself. These dividends are usually declared when the company has profits which,

v. Baltimore, &c., R. R. Co., 6 Gill, 368 (1848); *Scott v. Central Railroad, &c., Co. of Georgia*, 52 Barb. 45 (1868). So the Massachusetts Statute (Gen. Stat. ch. 47, §§ 23, 24), which provides that the income of any property, real or personal, given by will until the happening of a contingent event, shall be apportioned upon the happening of such event at any time before the end of a year from the time when the whole of the annual amount for the preceding year had become due, does not make apportionable dividends from the profits of business of incorporated companies not declared at the time when the event happened. *Granger v. Bassett*, 98 Mass. 462 (1868). *Acc. Goldsmith v. Swift*, 25 Hun, 201 (1881). Upon the general question of the relation of the shareholder to the property of the corporation, and especially to profits or undeclared dividends, see *City of Utica v. Churchill*, 33 N. Y. 161 (1875) [overruled in Supreme Court of the United States. *Van Allen v. Assessors*, 3 Wall. 573 (1865); *People v. Commissioners of Taxes*, 94 U. S. 415 (1876)]; *First National Bank v. Fancher*, 48 N. Y. 524 (1872); *Leitch v. Wells, Id.* 585 (1872); *North Hempstead v. Hempstead*, 2 Wend. 110 (1828); *Mickles v. Rochester City Bank*, 11 Paige, 118 (1844).

¹ *Elkins v. Camden, &c., R. R. Co.*, 36 N. J. Eq. 233 (1882).

² In *Ehle v. Chittenango Bank*, 24 N. Y. 548 (1862), where a dividend of the profits of a banking association was declared by the directors "payable in New York State currency," it was held that there was no authority any where to make it payable in anything else, and that evidence of an understanding by the cashier that "State currency" meant country bank notes current in New York city at a discount of a quarter of one per cent., in the absence of evidence to show a general usage in that sense, was inadmissible. In *Scott v. Central Railway, &c., Co. of Georgia*, 52 Barb. 45 (1868), the validity of dividends paid during the civil war, by southern corporations, in confederate money, is considered, the court holding that such dividends when expressly made payable in confederate money were valid and binding, even upon the northern shareholders of the company, but that dividends declared payable generally must be regarded as payable in lawful and not in unlawful money. The plaintiff, therefore, who sued as executor of a deceased shareholder, was allowed to recover the amount only of such dividends as had been declared without specific provision that they were to be paid in the current confederate currency. *Cf. Reid v. Eaton Manfg. Co.*, 40 Ga. 98 (1869).

however, are not in the shape of money, but are in other forms of property, and the company wishes to anticipate the time when the property may be sold for cash, and the cash distributed by a money dividend. The certificate sometimes entitles the holder to a sum of money payable with interest at a certain time after date, or at the option of the company, or when the company shall have accumulated sufficient surplus to pay the certificates in full. Sometimes the certificates are made convertible at the option of the holder into bonds or stocks,¹ or the certificate may entitle the holder to exchange the certificate for lands of the corporation to an amount equivalent in value to the face value of the certificate; or to receive from the corporation any other benefit or advantage which the corporation may lawfully confer. In issuing such certificates the corporation usually reserves the right to redeem them either at a fixed time or at its option, either in money or stock or bonds.² Sometimes the certificate so far partakes of the character of a certificate of stock that it entitles the holder to dividends.³ Where the corporation, having a large surplus, issues such certificates, they are held not to transfer the title to that surplus from the corporation to the holders of the certificates.⁴ In general the issue of scrip dividends is entirely lawful, and they are upheld by the courts, but when they are declared in fraud of the rights of third parties they may be set aside.⁵ A property dividend is rarely made, but in this country it would unquestionably be lawful, and is sometimes found convenient.⁶

¹ *Chaffee v. Rutland R. R. Co.*, 55 Vt. 110 (1882); *State v. Baltimore, & Co.*, 6 Gill, 363 (1848); *Brown v. Lehigh Coal Navigation Co.*, 49 Penn. St. 270 (1865); *Bailey v. Citizens Gas Light Co.*, 27 N. J. Eq. 196 (1876). See § 283.

² *Brown v. Lehigh Coal & Navigation Co.*, 49 Penn. St. 270 (1865).

³ *Bailey v. Railroad Co.*, 22 Wall. 604 (1874). *Cf. Brundage v. Brundage*, 60 N. Y. 544 (1875).

⁴ *People v. Board of Assessors*, 76 N. Y. 202 (1879); affirming s. c. 16 Hun, 196. In this case it was held that the issue of these certificates could not operate to relieve the corporation from their obligations to pay their tax upon the surplus, because the surplus remained in the hands of the company, and, as such, was liable to assessment and taxation. *Acc. Bailey v. Railroad Co.*, 22 Wall. 604

(1874). *Cf. Commonwealth v. Pittsburgh, & Co.*, R. R. Co., 74 Penn. St. 83 (1873).

⁵ While negotiations were pending between two gas companies for their consolidation, upon a certain basis of capital and indebtedness, one of them, without the knowledge of the other, passed a resolution declaring a scrip dividend of ten per cent. on its capital stock, thus increasing its indebtedness to that amount. The certificates were accordingly issued, but after the consolidation, upon a bill filed for that purpose, the scrip was declared void. *Bailey v. Citizens Gas Light Co.*, 27 N. J. Eq. 196 (1876).

⁶ In *Scott v. Central Railroad, & Co. of Georgia*, 52 Barb. 45 (1868), dividends paid during the civil war, by a Georgia corporation, in confederate currency, were upheld as though dividends of property.

§ 537. *Stock dividends*.—A stock dividend, as the name imports, is a dividend of the stock of the corporation. Such a dividend is lawful when an amount of money or property equivalent in value to the full par value of the stock distributed, as a dividend, has been accumulated and is permanently added to the capital stock of the corporation. Corporations frequently make a dividend of this character when improvements of the corporate property, or extension of the business, have been made out of profits earned, or when the corporate plant has increased in value, and it seems better to issue new stock to represent the excess of value, than to sell the increase and declare a cash dividend. In the United States these dividends are frequently made and are constantly sustained by the courts.¹ In general they can be initiated only by a vote of the shareholders, especially in a case where, as is usual, the power to increase the capital stock is vested exclusively in the body of stockholders.² But the

¹ *Williams v. Western Union Telegraph Co.*, 93 N. Y. 162, 188 *et seq.* (1883); *City of Ohio v. Cleveland, &c. R. R. Co.*, 6 Ohio St. 489 (1856); *Howell v. Chicago, &c. R. R. Co.*, 51 Barb. 378 (1868); *Clarkson v. Clarkson*, 18 Id. 646 (1855); *Simpson v. Moore*, 30 Id. 637 (1859); *Gordon's Executor v. Richmond, &c. R. R. Co.*, 78 Va. 501 (1884); *Minot v. Paine*, 99 Mass. 101 (1868); *Boston, &c. R. R. Co. v. Commonwealth*, 100 Id. 399 (1868); *Daland v. Williams*, 101 Id. 571 (1869); *Leland v. Hayden*, 102 Id. 542 (1869); *Rand v. Hubbell*, 115 Id. 461, 474 (1874); *Gibbons v. Mahon*, 4 Mackey, 130 (1885); *Jones v. Morrison*, 31 Minn. 140 (1883); *Earp's Appeal*, 28 Penn. St. 368 (1857); *Wiltbank's Appeal*, 64 Id. 256 (1870); *Commonwealth v. Pittsburgh, &c. R. R. Co.*, 74 Id. 83 (1873); *Biddle's Appeal*, 99 Id. 278; *Terry v. Eagle Lock Co.*, 47 Conn. 141 (1879); *Brander v. Brander*, 4 Vesey, Jur. 800 (1799); *Barton's Trust, L. R.* 5 Eq. 239. But see *Hoole v. Great Western Ry. Co.*, L. R. 3 Chan. 262 (1867). *Cf. Mills v. Northern Ry. of Buenos Ayres Co.*, L. R. 5 Chan. 621 (1870); *Brown v. Lehigh Coal & Nav. Co.*, 49 Penn. St. 270 (1865); *Moss' Appeal*, 83 Penn. St. 264 (1877); *Lord v. Brooks*, 52 N. H. 72 (1872); *Lohman v. New York, &c. R. R. Co.*, 2 Sandf. Super. Ct. 39 (1848); *Currie v. White*, 45 N. Y. 822 (1871); *State v. Baltimore, &c. R. R. Co.*, 6 Gill, 363 (1847). In *Kenton Furnace Railroad & Manfg. Co.*

v. McAlpin, 5 Fed. Rep. 737 (1880), it was held in the case of a Kentucky corporation, that an incorporated company, free from indebtedness, and acting in good faith, has the power, as between itself and its shareholders, all the shareholders assenting, to agree, in consideration of the surrender to it by the shareholders of accumulated profits, and of the increased value of the corporate plant and property, to treat stock upon which only fifty per cent. has been paid, as fully paid up stock, and to call in and cancel the original certificates, and issue in their stead new certificates for fully paid up stock—a transaction which was, in effect, simply the payment of an unpaid subscription out of accumulated profits. In Massachusetts, railway corporations are by statute prohibited from declaring a stock dividend, except by authority of the general court. Pub. Stat. of Mass., chap. 112, § 61. It has been held not a violation of this statute for a railway company to distribute among its shareholders without the assent of the general court, shares of its own stock which it had purchased from the commonwealth, when it had legislative authority for such purchase and distribution. *Commonwealth v. Boston & Albany R. R. Co.* (Mass. June 30, 1886) 25 Am. & Eng. Ry. Cas. 17. See §§ 51, 287.

² *Terry v. Eagle Lock Co.*, 47 Conn. 141 (1879); *Williams v. Western Union Telegraph Co.*, 93 N. Y. 162 (1883).

stock may lawfully be issued to the corporation, instead of to the stockholders, and subsequently sold for the benefit of the corporation.¹ The shareholders, having voted to declare such a dividend, may, at any time before the certificates are issued, reconsider the matter, and revoke the dividend.² In Virginia, in a recent case, it is declared that the holders of preferred stock are entitled to share equally with the common stockholders in a distribution of stock by a stock dividend; that the preferred stockholders are entitled first to their dividends, in full before the common stockholders are paid anything, and then after the dividends are paid on the common stock, to any other or further distribution of profits equally with the holders of the common stock.³

§ 538. *Interest-bearing stock.*—It has already been shown elsewhere that a corporation may issue stock and contract with the subscriber that the company will pay interest upon the sums paid in by the subscriber.⁴ Such a contract is legal, however, only when the interest is to be paid from the net profits of the enterprise, and not from the capital stock. Unless net profits have been earned, the stipulated interest cannot legally be paid. Consequently there is little difference between interest-bearing stock, and preferred stock.

§ 539. *Dividends can be made only from net profits—Net profits defined.*—A dividend can lawfully be made only out of net profits. The payment of it must leave the capital stock of the company intact and unimpaired, or it will be held fraudulent and void.⁵

¹ Jones v. Morrison, 31 Minn. 140 (1883).

² Terry v. Eagle Lock Co., *supra*.

³ Gordon's Executors v. Richmond, &c. R. R. Co., 78 Va. 501 (1884); s. p. Phillips v. Eastern R. R. Co., 138 Mass. 122 (1884).

⁴ See § 277, *supra*.

⁵ Lockhardt v. Van Alstyne, 31 Mich. 76 (1875); Attorney General v. State Bank, 1 Dev. & B. (N. C. Eq.) 545, 555 (1837); Elkins v. Camden, &c. R. R. Co., 36 N. J. Eq. 233 (1882); Carpenter v. New York, &c. R. R. Co., 5 Abb. Prac. 277 (1857); Hughes v. Vermont Copper Mining Co., 72 N. Y. 207, 210 (1878); Pittsburgh, &c. R. R. Co. v. County of Allegheny, 63 Penn. St. 126 (1869). In deciding whether a dividend was rightfully made,

the transaction must be viewed from the standpoint of that time, and not in the light of subsequent events. Notes or overdrafts by persons then considered abundantly good, included among the corporate assets when the dividend was declared and paid, should not be regarded as losses sustained by the corporation, because they afterwards proved to be unavailable. Main v. Mills, 6 Biss. 98 (1874). *In re Mercantile Trading Co.*, L. R. 4 Chan. 475 (1869); *Cf.* Fliteroff's Case, L. R. 21 Chan. Div. 519 (1882). Accordingly, it is held that dividends made and paid in good faith when the company is solvent, cannot be reached by corporate creditors, upon the subsequent insolvency of the company. Reid v. Eatonton Manufg. Co., 40 Ga. 98 (1869).

A court of chancery will, upon the application of any dissenting member, enjoin an attempt to distribute any part of the capital stock as a dividend.¹ But it has been held that an injunction will not be granted, at the instance of corporate creditors, to restrain the payment of such a dividend, or other acts tending to decrease the amount of corporate assets.² Nor will equity restrain the payment of a dividend merely upon allegations that an account, honestly made out, and published in good faith, contains certain immaterial errors in calculation,³ or that there is not actually cash in hand or at the banker's to the full amount of the proposed dividend.⁴ The facts may be such that equity would restrain the declaration of the dividend, but not the payment of it after it had been declared.⁵ But, except in cases of fraud injuriously affecting citizens of this State, said the Supreme Court of New York, our courts will not enjoin the payment of dividends by foreign corporations.⁶

The payment of a dividend out of the capital stock is *ultra vires*, and incapable of ratification by the shareholders. Accordingly, where the directors mislead the shareholders by representing in the reports and balance sheets as good, debts which they know to be bad, and thus knowingly pay dividends which in fact impair the capital stock, it is not a defense that the shareholders, relying in good faith upon the representations and reports of the directors, pass resolutions declaring the dividends at regular meetings of the corporation, and an action will lie on behalf of creditors to compel the directors to refund. In such an action the directors cannot set off any money due from the company to them, nor have they recourse to the shareholders who took the dividends *bona fide*. *In re Exchange Banking Co.*, L. R. 21 Chan. Div. 519 (1882); *Acc. Main v. Mills*, 6 Biss. 98 (1874); *In re County Marine Ins. Co.*, L. R. 6 Chan. 104 (1870). See also *Scott v. Eagle Fire Ins. Co.*, 7 Paige 198 (1838). In New York the statutes provide very explicitly as to the declaration of dividends by moneyed corporations, and as to the manner in which surplus profits are to be ascertained, Rev. Stat. of New York, Chap. XVIII, title 2, art. 1, § 3 (seventh ed. 1865); *Idem*, title 4, § 2 (seventh ed., p. 1533).

¹ *Macdougall v. Jersey Imperial Hotel*

Co., 2 Hem. & M. 528 (1864); *Bloxam v. Metropolitan Ry. Co.*, L. R. 3 Chan. 337 (1867); *Salisbury v. Metropolitan Ry. Co.*, 38 L. J. Chan. 249 (1869); *Carpenter v. New York, &c., Ry. Co.*, 5 Abb. Prac. 277 (1857).

² *Mills v. Northern Ry. of Buenos Ayres Co.*, L. R. 5 Chan. 621 (1870).

³ *Yool v. Great Western Ry. Co.*, 20 T. L. (N. S.) 74 (1869). But it is otherwise when there is an intentional misrepresentation. *Rance's Case*, L. R. 6 Chan. 104 (1870).

⁴ *Stringer's Case*, L. R. 4 Chan. 475 (1869).

⁵ *Carpenter v. New York, &c., R. R. Co.*, 5 Abb. Prac. 277 (1857). In *Carlisle v. Southeastern Ry. Co.*, 1 MacN. & G., 689 (1850), upon a bill filed to restrain the railway company from paying any dividend, either declared or to be declared, contrary to the provisions of an Act of Parliament, it was held proper to grant the injunction as to future dividends, but to refuse it as to a dividend declared, on the ground that the plaintiff showed no title to share in such dividend, and that the general body of the shareholders who were interested in the dividend was not adequately represented. But see *Browne v. Monmouthshire Ry. & Canal Co.*, 13 Beav. 32 (1851); *Coates v. Nottingham Waterworks Co.*, 30 Id. 86 (1861).

⁶ *Howell v. Chicago, &c., R. R. Co.*,

§ 540. In view of the rule that dividends can be made only from net profits, it becomes important to ascertain, as precisely as possible, what part of the income of a corporation will lawfully constitute such "net profits." This question seems to have caused the courts considerable difficulty. Mr. Justice Blatchford, by way of a definition, having special reference to the case of the net profits and net earnings of a railway company, says: "Net earnings are, properly, the gross receipts, less the expenses of operating the road to earn such receipts. Interest on debts is paid out of what thus remains, that is, out of net earnings. Many other liabilities are paid out of the net earnings. When all liabilities are paid, either out of the gross receipts or out of net earnings, the remainder is the profit of the shareholders, to go towards dividends, which in that way are paid out of the net earnings."¹

51 Barb. 378 (1868). In Massachusetts no equitable relief can be granted against a foreign corporation, which has neither officers nor place of business in that State, for a failure to declare and pay dividends according to the stipulations of their certificates of stock. *Williston v. Michigan Southern, &c., R. R. Co.*, 13 Allen, 400 (1866). In Virginia it is the rule that interest upon guaranteed stock is to be paid out of the gross earnings of the corporation. *Gordon's Executors v. Richmond, &c., R. R. Co.*, 78 Va. 501 (1884). See Ch. XVI.

¹ *St. John v. Erie Ry. Co.*, 10 Blatchf. 271, 279; s. c. aff'd, 22 Wall. 136 (1874); *Warren v. King*, 108 U. S. 389 (1882). *Of. Union Pacific R. R. Co. v. United States*, 99 U. S. 402, 418 (1878). Net earnings, it is clear, are one thing, and not at all the same thing as net profits. *People v. Supervisors of Niagara*, 4 Hill, 20, 23 (1842). See *Park v. Grant Locomotive Works*, 40 N. J. Eq. 114 (1885). "Surplus earnings" are said to be net profits in *Williams v. Western Union Telegraph Co.*, 93 N. Y. 162, 191 (1883). See *Union Pacific R. R. Co. v. United States*, 99 U. S. 402 (1878). And in *Van Dyck v. McQuade*, 86 N. Y. 38, 47 (1881), it is held that savings banks organized under the act of 1875 (Laws of 1875, ch. 371), can lawfully pay dividends only from surplus profits, which, as the statute itself provides (Laws of 1875, chap. 371, § 3), are to be ascertained by deductions

from "actual profits," "the interest paid or then due or accrued on debts owing by the company." "Net earnings" is a term synonymous with "net income." *Phillips v. Eastern R. R. Co.*, 138 Mass. 122 (1884). In *Belfast, &c., R. R. Co. v. Belfast*, 77 Me. 445 (1885), it is said that the term "net earnings" does not imply that the company is wholly out of debt; and in *Myles v. Northern, &c., Ry. Co.*, L. R. 5 Chan. Ap. 621 (1870), Lord Hath-erly, L. C., said: "Mr. Dickinson started a very curious theory, which, I apprehend, never found its way into any mercantile arrangement—that there never can be any available income, or any profit, so long as there is any debt remaining unpaid. If that be so, I suppose there is, hardly a railway in the kingdom which could pay any dividends at all to their stockholders." In *Barry v. Merchants Exchange Co.*, 1 Sandf. Chan. 280, 307, (1844), Vice-Chancellor Sandford says, "The capital stock of a corporation is, like that of a copartnership or joint-stock company, the amount which the partners or associates put in as their stake in the concern. To this they add upon the credit of the company, from the means and resources of others, to such an extent as their prudence or the confidence of such other persons will permit. Such additions create a debt; they do not form capital. And if successful in their career, the surplus over and above their capital and debts becomes profits, and is either

It is not required that a corporation be entirely free from debt before it may lawfully make a dividend to its shareholders.¹ And it may properly borrow money to pay a dividend, if, upon a fair estimate of its assets and liabilities, it has assets in excess of its liabilities equal to the amount of the proposed dividend.² Unearned premiums received by an insurance company, on which the risks are still running, are not surplus profits out of which dividends can legally be made without leaving a sufficient surplus on hand to meet the probable losses on risks then assumed and not yet terminated, independent of the capital stock of the corporation.³ The term net profits has been held to mean net earnings after deducting current working expenses, without including interest on money borrowed,⁴ and also to mean that which remains after the deduction of all charges and every outlay.⁵ But, upon a reduction of the capital stock, the surplus funds over and above the full amount of the capital stock, as reduced, may be divided among the stockholders, the only restriction being that such a distribution leave the reduced capital stock entire and unimpaired.⁶ The surplus earnings of an insolvent concern cannot legally be distributed as a dividend.⁷ When the company

divided among the partners and associates or used still further to extend their operations."

¹ *Mills v. Northern Railway of Buenos Ayres Co.*, L. R. 5 Chan. 621 (1870).

² *Stringer's Case*, L. R. 4 Chan. 475 (1869). Funds on hand—a cash balance in bank to the credit of the corporation—the total indebtedness of the company being less in amount than the balance, are not such net profits as will justify a court to order a dividend to be declared. *Karnes v. Rochester, &c.*, R. R. Co., 4 Abb. Prac. (N. S.) 107 (1867).

³ *De Peyster v. American Fire Ins. Co.*, 6 Paige, 486 (1837). *Acc. Scott v. Eagle Fire Ins. Co.*, 7 Id. 198 (1838); *Lexington, &c., Ins. Co. v. Page*, 17 B. Mon. 412 (1856). In *Gratz v. Redd*, 4 B. Mon. 178, 187 (1843), it is held that capital stock, paid in for the purpose of carrying into effect the objects of the company, does not, upon a forfeiture of the stock, become profits, and liable to be distributed as a dividend. Money paid in as capital must remain, and be treated and expended as capital, whether the stock that represents it is forfeited or not. To distribute such money as profits is to squander and dissipate the capital stock.

In the following cases the term "net profits," or an equivalent phrase, is defined. *Coltness Iron Co. v. Black*, 51 L. J. (Q. B. Div.) 626 (1881); *Nickals v. New York, &c., R. R. Co.*, 21 Blatchf. 177 (1883); s. c., 15 Fed. Rep. 575; *Heard v. Eldredge*, 109 Mass. 258; *Bloxam v. Metropolitan Ry. Co.*, L. R. 3 Chan. 337 (1867); *Salisbury v. Id.*, 38 L. J. Chan. 249 (1869); *Bardwell v. Sheffield Waterworks Co.*, L. R. 14 Eq. 517 (1872); *Park v. Grant Locomotive Works*, 40 N. J. Eq. 114 (1885).

⁴ *Corry v. Londonderry, &c., Ry. Co.*, 29 Beav. 263 (1860). *Cf. People v. The Supervisors*, 4 Hill, 20 (1842).

⁵ *St. John v. Erie Ry. Co.*, 22 Wall. 136 (1874). *Cf. Warren v. King*, 108 U. S. 389 (1882).

⁶ *Seeley v. New York National Exchange Bank*, 8 Daly, 400 (1877); s. c., *Thompson Natl. Bank Cas.*, 804; *aff'd*, 78 N. Y. 608 (1879); *Strong v. Brooklyn Crosstown R. R. Co.*, 93 N. Y. 426, 435 (1883); *Parker v. Mason*, 8 R. I. 427 (1867). See also § 548.

⁷ The directors of a joint-stock insurance corporation may be compelled to divide the actual surplus profits of the company among its shareholders from

has used profits for improvements, it may lawfully borrow an equivalent sum of money for the purpose of a dividend.¹ And profits earned and accumulated in times of prosperity may properly be paid out as dividends subsequently and at a time when no dividends have been earned.² Where, however, a consolidation takes place, it is unlawful to take the profits of any of the old corporations for a dividend to the shareholders of the new organization. Such profits belong exclusively to the shareholders of the corporation by which they were earned.³

§ 541. *Discretion of the directors as to declaring dividends.*

—In general it is for the directors, and not the shareholders, to determine whether or not a dividend is to be declared. When, therefore, the directors have exercised this discretion, and declared or refused to declare a dividend, there will be no interference by the courts with their decision, unless they are guilty of a willful abuse of their discretionary powers, or of bad faith, or of a neglect of duty.⁴ Accordingly, the directors may, in the

time to time, if they neglect or refuse to do so without any reasonable cause. But if they abuse their power to make dividends out of surplus profits, by dividing the unearned premiums received by them without leaving a sufficient fund, exclusive of the capital stock, to satisfy the probable losses upon risks assumed by the company, they will be personally liable to the creditors of the company, if, in consequence of extraordinary losses, the company becomes insolvent and be unable to pay its debts. *Scott v. Eagle Fire Ins. Co.*, 7 Paige, 198 (1838). *Cf. Karnes v. Rochester, &c., R. R. Co.*, 4 Abb. Prac. (N. S.) 107 (1867).

¹ *Mills v. Northern Railway of Buenos Ayres Co.*, L. R. 5 Chan. 621 (1870); *Stringer's Case*, L. R. 4 Chan. 475 (1869).

² *Mills v. Northern Railway of Buenos Ayres Co.*, *supra*. *Cf. Hoole v. Great Western Ry. Co.*, L. R. 3 Chan. 262 (1867); *Beers v. Bridgeport Spring Co.*, 42 Conn. 17 (1875).

³ *Chase v. Vanderbilt*, 37 N. Y. Super. Ct. 334 (1874). In *March v. Eastern R. R. Co.*, 43 N. H. 515 (1862), where one railroad leased its entire property and franchises to another, it was held that, under the provisions of the lease, there was neither a union of interest and capital between the two roads, nor any warrant of an equality of dividends between the stockholders of the two corporations.

⁴ *Howell v. Chicago, &c., R. R. Co.*, 51 Barb. 378 (1868); *Ely v. Sprague, Clarke's Chan. (N. Y.)* 851 (1840); *Scott v. Eagle Fire Ins. Co.*, 7 Paige, 198 (1838); *Williams v. Western Union Telegraph Co.*, 93 N. Y. 162 (1883); *Park v. Grant Locomotive Works*, 40 N. J. Eq. 114 (1885); *Barnard v. Vermont, &c., R. R. Co.*, 7 Allen, 512 (1863); *Chaffee v. Rutland R. R. Co.*, 55 Vt. 110 (1882); *Smith v. Prattville Manfg. Co.*, 29 Ala. 503 (1857). See also *Barry v. Merchants Exchange Co.*, 1 Sandf. Chan. 280 (1844); *Luling v. Atlantic Mutual Ins. Co.*, 45 Barb. 510 (1865); *Jackson's Admr. v. Newark Plankroad Co.*, 31 N. J. Law, 277 (1865); *The King v. Bank of England*, 2 Barn. & Ald. 620 (1819); *Stringer's Case*, L. R. 4 Chan. 475 (1869); *Browne v. Monmouthshire Ry. & Canal Co.*, 4 Eng. Law & Eq. 118; s. c., 13 Beav. 32 (1851). The directors are bound to distribute as profits only such part of the net income as they think proper, and their judgment of what is proper is conclusive upon the stockholders. *State v. Baltimore, &c., R. R. Co.*, 6 Gill, 363 (1848); *State of Louisiana v. Bank of Louisiana*, 6 La. 745 (1834). In consequence, an action at law cannot be maintained against a corporation by one of its stockholders to compel it to declare and pay a dividend from funds on hand. *Karnes v. Rochester, &c., R. R. Co.*, 4

fair exercise of their discretion, invest profits to extend and develop the business,¹ or retain profits in the treasury as a fund to meet probable or possible liability upon disputed claims,² or for the payment of probable future indebtedness, though it is not yet contracted.³ The free exercise of their discretion cannot be interfered with by the contracts of promoters or original incorporators as to the disposition of corporate profits.⁴ But when money which ought to have been divided among the shareholders has been applied by the directors to a purpose not warranted by, and not within the scope of the charter, there is such a breach of trust as to give a court of equity jurisdiction.⁵ And, obviously, whenever there is a clear abuse of power on the part of the corporate management, and a refusal to declare a dividend that ought to be

Abb. Prac. (N. S.) 107 (1867). In this case it is held that a corporation stands in no fiduciary relation to its stockholders. The directors, not the corporation, are the trustees, and they should be the parties defendant to a suit for the enforcement of the trust. But compare *Brown v. Buffalo, &c., R. R. Co.*, 27 Hun, 342 (1882). A very strong case must be made to require a court to interfere with the direction of the directors in relation to the *quantum* of profits of the corporation which they are to divide as dividend. *State of Louisiana v. Bank of Louisiana*, 6 La. 745 (1834). In *Lambert v. Neuchatel Asphalt Co.*, 51 L. J. Chan. 882 (1882), where a company having a capital stock, divided into both preference and ordinary shares, was authorized by its articles to divide its "net profits," in certain proportions, between the two classes of shareholders, and to set aside a certain part of the net profits for a reserve fund; in an action by an ordinary shareholder, to prevent the payment of a dividend which had been declared on the preference shares, until certain extraordinary indebtedness of the company had been paid, it was held that a court of chancery had no power to interfere, because, by the articles of association, the interpretation of the term "net profits" had been left to the company in general meeting, and the other questions involved in the making of a dividend to the directors, and that, in consequence, in the absence of fraud, when the company and directors had settled upon a dividend, their decision was not subject to a review in chancery. *Cf. Dent v. London Tram.*

ways Co., 50 L. J. Chan. 190 (1880); s. c. L. R. 16 Chan. Div. 344; *Davison v. Gillies*, Id. 192, note (1879); *Coltness Iron Co. v. Black*, 51 L. J. Q. B. Div. 626 (1881); *Park v. Grant Locomotive Works*, 40 N. J. Eq. 114 (1885).

¹ Where a corporation having a large surplus proposed, with the concurrence of a majority of the shareholders, to employ the surplus in extending the business, although such extension was opposed by a minority of the shareholders, it appearing that the proposed enlargement of the corporate enterprise was clearly *intra vires*, and that the nominal capital of the company was in reality much less than the amount constantly used and necessary for its ordinary operations, it was held, on a bill brought by the dissenting minority for an injunction against the proposed use of the surplus, and praying a distribution of it among the shareholders, that the facts were not such as to require the interposition of the court on behalf of the minority. *Pratt v. Pratt*, 33 Conn. 446 (1866). *Cf. Park v. Grant Locomotive Works*, 40 N. J. Eq. 114 (1885).

² *Carpenter v. New York, &c., R. R. Co.*, 5 Abb. Prac. 277 (1857).

³ *Karnes v. Rochester, &c., R. R. Co.*, 4 Abb. Prac. (N. S.) 107 (1867).

⁴ *Coyote Gold & Silver Mining Co. v. Ruble*, 8 Oregon, 284 (1880). *Cf. Richardson v. Railroad Company*, 44 Vt. 618 (1872).

⁵ *March v. Eastern R. R. Co.*, 43 N. H. 515 (1862); *Park v. Grant Locomotive Works*, 40 N. J. Eq. 114 (1885).

declared, a court of equity will, at the instance of any shareholder, compel the proper authorities to declare and pay the dividend.¹ Laches on the part of the shareholders, in failing to commence their suit to compel the payment of a dividend until the corporation becomes insolvent, is fatal.² And the court will also consider, as against an enforcement of the dividend, that the aggrieved shareholders may, if a majority, refuse to re-elect the directors at the next election, or that the complaining stockholders may sell their shares.³

§ 542. *To whom the dividend is to be paid.*—The question to whom shall the dividend be paid after it has been regularly declared, is one which sometimes involves the corporate management in considerable difficulty. It is not always easy to decide which one of two or more claimants is entitled to the dividend. The *cestui que trust* may claim it as against the trustee; the heir or distributee as against the executor or administrator; or the unrecorded transferee as against the owner of the record. In these and like cases of disputed titles to dividends the general rule is that the corporation may lawfully pay, and may safely pay the dividend to the person in whose name the stock stands registered upon the corporate stock book.⁴ It may do so without inquiring whether he has transferred the stock,⁵ and without requiring the production of the certificate.⁶ It is a well settled rule that the corporation is protected in paying dividends to a recorded shareholder, although he may have transferred his shares.⁷ But after notice of a transfer the corporation may properly pay the

¹ *Stevens v. South Devon Ry. Co.*, 9 Hare, 313 (1851); *Browne v. Monmouthshire Ry. & Canal Co.*, 4 Eng. L. & E. 118; s. c., 13 Beav. 32 (1851); *Brown v. Buffalo, &c., R. R. Co.*, 27 Hun, 342 (1882); *Park v. Grant Locomotive Works*, 40 N. J. Eq. 114 (1885); *Scott v. Eagle Fire Ins. Co.*, 7 Paige, 198 (1838); *State of Louisiana v. Bank of Louisiana*, 6 La. 745 (1834); *Pratt v. Pratt*, 33 Conn. 446 (1866); *Beers v. Bridgeport Spring Co.*, 42 Id. 17 (1875).

² *Scott v. Eagle Fire Ins. Co.*, *supra*.

³ *Barry v. Merchants Exchange Co.*, 1 Sandf. Chan. 280 (1844).

⁴ *Brisbane v. Delaware, &c. R. R. Co.*, 94 N. Y. 204 (1883); *aff'd* 25 Hun, 438 (1881); *Smith v. American Coal Co.*, 7 Lansing, 317 (1873); *Jones v.*

Terre Haute, &c. R. R. Co., 29 Barb. 353 (1859); *Northrup v. Newtown, &c. Turnpike Co.*, 3 Conn. 544 (1821). *Cf. Manning v. Quicksilver Mining Co.*, 24 Hun, 360 (1881); *McNeil v. Tenth National Bank*, 46 N. Y. 325 (1871); *Bank of Utica v. Smalley*, 2 Cowen, 770 (1824).

⁵ *Cleveland, &c. R. R. Co. v. Robbins*, 35 Ohio St. 483 (1880); *Brisbane v. Delaware, &c. R. R. Co.*, 25 Hun, 438 (1881); *Bank of Commerce's Appeal*, 73 Penn. St. 59 (1873); *Bell v. Lafferty*, 1 Penn. Sup. Court, 454 (1881).

⁶ *Brisbane v. Delaware, &c. R. R. Co.*, 94 N. Y. 204 (1883); *Cleveland, &c. R. R. Co. v. Robbins*, 35 Ohio St. 483 (1880).

⁷ *Cleveland, &c. R. R. Co. v. Robbins*, *supra*.

dividend to the transferee, although no registry has been made.¹ And between two claimants of the dividend, one being the *cestui que trust* and the other a *bona fide* transferee, the corporation may interplead.² When a dividend is made payable on a day subsequent to the day on which it is formally declared, it belongs to the stockholder who owns the shares on the day the dividend is declared, and not to the owner when it is payable.³ A transfer of stock passes all dividends declared subsequently to the transfer, although the dividend was earned before the transfer was made.⁴ And a purchaser of stock at a tax sale, if the proceedings are legal and regular on their face, is entitled to a certificate and to dividends subsequently declared.⁵ The right to dividends does not, however, depend upon the issue of the certificate, and the owner of shares may claim his dividends though no certificate has ever been issued by the corporation.⁶ The heirs of a stockholder must, in order to entitle themselves to dividends, procure a transfer of their ancestor's shares into their own names on the

¹ Bell v. Lafferty, 1 Penn. Sup. Court, 454 (1881); Hill v. Newichawanick Co., 48 How. Prac. 427 (1874). See Smith v. American Coal Co., 7 Lansing, 317 (1873), and cf. Bank of Utica v. Smalley, 2 Cowen, 770 (1824).

² Salisbury Mills v. Townsend, 109 Mass. 115 (1871).

³ Wright v. Tuckett, 1 Johns. & H. 266 (1860); De Gendre v. Kent, L. R. 4 Eq. 283 (1867); Hill v. Newichawanick Co., 71 N. Y. 593 (1877); affirming, s. c., 8 Hun, 459; 48 How. Prac. 427 (1874); Spear v. Hart, 3 Robertson, 420 (1865); Bright v. Lord, 51 Ind. 272 (1875). Cf. Brundage v. Brundage, 60 N. Y. 544 (1875); affirming, s. c., 65 Barb. 397 (1873); Hopper v. Sage, 47 N. Y. Super. Ct. 77; Manning v. Quicksilver Mining Co., 24 Hun, 360 (1881); City of Ohio v. Cleveland, &c. R. R. Co., 6 Ohio St. 489 (1856); Clive v. Clive, Kay (Eng. Chan.), 600 (1854). *Contra*, Burroughs v. North Carolina R. R. Co., 67 N. C. 376 (1872).

⁴ Kane v. Bloodgood, 7 Johns. Chan. 90 (1823), by Chan. Kent; Bailey v. Railroad Co., 22 Wall. 604, 637 (1874). A dividend belongs to the owners of the stock at the time the dividend is declared. Goodwin v. Hardy, 57 Me. 143 (1869); Marsh v. Eastern R. R. Co., 43 N. H. 515 (1862); State of Louisiana v. Bank of Louisiana, 6 La. 745 (1834), although the fund from which it was de-

clared was earned in great part before they became stockholders. Phelps v. Farmers & Mechanics Bank, 26 Conn. 269 (1857); Brundage v. Brundage, 1 Thomp. & C. (N. Y. Sup. Ct.) 82 (1873); Jones v. Terre Haute, &c. R. R. Co., 57 N. Y. 196 (1874); Currie v. White, 45 Id. 822 (1871). A dividend belongs to the owner of the stock at the time the dividend accrues. Dow v. Gould and Curry Silver Mining Co., 31 Cal. 629 (1867). Mere possession of the stock or a special property therein is not sufficient to entitle one to dividends. The surplus profits of a corporation, whenever they accrued, are to be distributed among such persons as are stockholders when the dividend is declared. Goodwin v. Hardy, 57 Me. 143 (1869); Hill v. Newichawanick Co., 48 How. Prac. 427 (1874). The profits and surplus funds of a corporation whenever they may have accrued are, until separated from the capital by the declaring of a dividend, a part of the stock itself, and will pass under that name in a transfer or bequest. Phelps v. Farmers & Mechanics Bank, 26 Conn. 269 (1857). Cf. Clapp v. Astor, 2 Edw. Chan. 379 (1834).

⁵ Smith v. Northampton Bank, 4 Cush. 1 (1849, Shaw, C. J.)

⁶ Ellis v. Proprietors of Essex Merrimack Bridge, 2 Pick. 243 (1824).

corporate books.¹ Moreover, the corporation is protected if it pay dividends to the administrator without notice of a transfer by him.² With respect to the dividends on the stock of a married woman, the corporation must pay them to the husband or not, according to the law of the domicile of the corporation, and not at all according to the law of the domicile of the married woman.³ And the husband by collecting dividends on his wife's shares does not thereby reduce the stock to possession.⁴ Without, perhaps, a positive declaration in its favor, there is a plain tendency to hold that the custom of closing the transfer books for a certain number of days before a dividend is paid, is a lawful and regular exercise of control over the corporate affairs on the part of the management.⁵

§ 543. *To whom the dividend belongs.*—As between the vendor and vendee of shares of stock, it is a settled rule that the vendee is entitled to all the dividends on the stock which are declared after the transfer of the certificate of stock. Even though the transfer has not been recorded the transferee has a right to the dividends as against the transferor. The law, moreover, refuses to investigate the question when the dividend was earned. In contemplation of law the net profits were earned at the instant the dividend is declared.⁶ But of course any agreement in other respects valid between vendor and vendee, modifying or

¹ *State v. New Orleans, &c. R. R. Co.*, 30 La. Ann. 308 (1878).

² *Brisbane v. Delaware, &c. R. R. Co.*, 94 N. Y. 204 (1883).

³ *Graham v. First National Bank of Norfolk*, 84 N. Y. 393 (1881); affirming, s. c., 20 Hun. 325. *Cf. Dow v. Gould & Curry Silver Mining Co.*, 31 Cal. 629 (1867).

⁴ *Burr v. Sherwood*, 3 Bradf. (N. Y. Surrogate), 85 (1854). *Cf. Harcum v. Hudnall*, 14 Gratt. 369, 382 (1858); *Searing v. Searing*, 9 Paige, 283 (1841); *Hart v. Stephens*, 6 Adol. & Ellis (N. S.) 937 (1845). A receipt of dividends by the husband only reduces the dividends into possession and not the stock. See § 319.

⁵ *Jones v. Terre Haute, &c. R. R. Co.*, 57 N. Y. 196, 205 (1874). This right is frequently given to the corporation by its charter.

⁶ *King v. Follett*, 3 Vt. 385 (1831); *Abercrombie v. Riddle*, 3 Md. Chan. 320

(1850); *Central R. R. and Banking Co. of Ga. v. Papot*, 59 Ga. 342 (1877); *Ryan v. Leavenworth, &c. R. R. Co.*, 21 Kan. 365, 403 (1879); *Foot, Appellant*, 22 Pick. 299 (1839); *Jones v. Terre Haute, &c. R. R. Co.*, 57 N. Y. 196 (1874); *Currie v. White*, 45 Id. 822 (1871); *Brundage v. Brundage*, 65 Barb. 397, 408 (1873); *Goodwin v. Hardy*, 57 Me. 143 (1869); *Hill v. Newichawanick Co.*, 48 How. Prac. 427 (1874); *Black v. Homersham*, L. R. 4 Exch. Div. 24 (1878); *Bates v. McKinley*, 31 L. J. Chan. 389 (1862). *Cf. Union Screw Co. v. American Screw Co.*, 11 R. J. 569 (1877); s. c., aff'd, 13 Id. 673 (1880); *Kane v. Bloodgood*, 7 Johns. Chan. 90 (1823); *Coleman v. Columbia Oil Co.*, 51 Penn. St. 74 (1865); *Minot v. Paine*, 99 Mass. 101 (1868); *Boston, &c. R. R. Co. v. Commonwealth*, 100 Id. 599 (1868); *Gifford v. Thompson*, 115 Id. 478 (1874). A purchaser of shares of stock takes the shares with all their incidents,

changing this rule, will be upheld. It is a proper subject for a contract, and a valid contract may be made in reference to it.¹ But where such an agreement exists there is still a presumption that the general rule is to prevail, and that the dividend is not apportionable.²

A legatee of shares takes the stock as it was at the time of the testator's death. All dividends declared previous to that event go to the administrator.³ Where stock is bought, deliverable at the seller's option, the dividends declared between the

one of which is the right to receive all future dividends declared on the shares. Nor does it make any difference at what times or from what sources the profits which constitute the dividend may have accrued. They are an incident to the shares to which the purchaser becomes at once entitled, provided only that he remain a member of the corporation until a dividend is made. *March v. Eastern R. R.*, 43 N. H. 515 (1862). In *Clive v. Clive*, Kay (Eng. Chan.), 600 (1854), by the terms of the deed of settlement the net profits of the concern were to be divided ratably to such an amount as should be declared at the semi-annual meetings, and were to be paid within twenty-one days thereafter, and it was provided that a shareholder was not to receive any dividend after the period at which he ceased to be a proprietor of shares, but the dividends on such shares were to continue in suspense until some other person should become proprietor of them. When a shareholder died sixty-nine days after a half-yearly meeting at which a dividend had been declared, but before notice had been given that such dividend was payable, having by his will bequeathed the interest and annual income arising from all his shares, to one for life—and then in remainder to others—it was held that this dividend belonged to the legatee for life, and not to the general personal estate of the testator. See also *Title to Dividends*, 19 Am. Law Rev. 571 (1885).

¹ *Brewster v. Lathrop*, 15 Cal. 21 (1860); *Hyatt v. Allen*, 56 N. Y. 553 (1874).

² Thus, for example, a bequest of the income of shares in a corporation to the testator's widow for life, for her own maintenance and the support and education of her children, includes a dividend

declared thereon after her death for a period that expired during her life, although the shares still stood in the name of the testator's estate, and her executor after demand may maintain an action for such dividend against the corporation. *Johnson v. Bridgewater Iron Manfg. Co.*, 14 Gray, 274 (1859). Where it is agreed that a party shall receive all dividends and profits on certain stock so long as he remain in a designated employment, and he leaves the employment before any dividend is made, he cannot have any apportionment of any general dividend afterwards made. Profit does not become dividend until so declared by the directors. *Clapp v. Astor*, 2 Edw. Chan. 379 (1834). In this case preferred stock was issued under an agreement entitling the holders to non-cumulative dividends in preference to the common stock, but dependent upon the profits of each particular year, as declared by the board of directors, and the board in their report for a certain year stated that there had been a net profit more than sufficient to pay the dividend on the preferred stock, but resolved that they did not deem it wise to declare the dividend, and subsequently applied the net profit to the permanent improvement of the property. It was held, in an equitable action by the holders of the preferred stock, which had been transferred to them after the year in question, that the complainants were entitled to a decree that the net profits of that year be ascertained and the dividends due to the holders of the preferred stock be paid. *Nickals v. New York, Lake Erie & Western Ry. Co.*, 21 Blatchf. 177 (1883); s. c., 15 Fed. Rep. 575, 15 Rep 72.

³ *Brundage v. Brundage*, 60 N. Y. 544 (1875). Cf. *Johnson v. Bridgewater Iron Mfg. Co.*, 14 Gray, 274 (1859).

day of the purchase and the delivery belong to the purchaser.¹ So also an offer to sell shares, which is subsequently accepted, entitles the vendee to dividends received by the owner while the offer was open.² But a contract to sell on demand entitles the vendor to dividends declared before the demand is made.³

Considerable difficulty has been experienced in determining to whom the dividend belongs when it was declared before, but made payable after the day of the sale. According to the more general rule it belongs to the vendor,⁴ but there are cases in which the right of the vendee to such dividends is maintained.⁵ A dividend declared but payable at a future day, may be assigned apart from the stock itself.⁶

§ 544. *Dividends must be equal and without preferences.*—Dividends among stockholders of the same class must be always

¹ Currie v. White, 45 N. Y. 822 (1871). In this case it is held that a contract for the purchase and sale of shares of the stock of a railroad corporation, at a specified price, "payable and deliverable, seller's option, in this year, with interest at the rate of six per cent. per annum," effects a sale *in presenti*, the vendor becoming a *quasi* trustee for the purchaser, and the latter is entitled to all dividends accruing on such shares thereafter. And the case is all the stronger when a deposit is paid upon the sale. Black v. Homersham, L. R., 4 Exch. Div. 24 (1878).

² Harris v. Stevens, 7 N. H. 454 (1835).

³ Bright v. Lord, 51 Ind. 272 (1875). Cf. Central R. R. & Banking Co. of Ga. v. Papot, 59 Ga. 342 (1877). In Southwestern R. R. Co. v. Papot, 67 Ga. 675, 690 (1881), where stock had been advanced to a construction company, upon an agreement of the contractors to account for the accruing dividends upon a final settlement, it was held that such agreement was not the same thing as to agree to pay interest on the amount of stock advanced before the road was completed, even though the rate of interest may be the same per cent. as the rate of dividends, because in the one case the presumption that dividends follow the ownership of the stock is to be overcome, and in the other it is not.

⁴ Hill v. Newichawanick Co., 8 Hun, 459 (1876); s. c. 45 How. Prac. 427 (1874); aff'd, 71 N. Y. 593 (1877); Boardman v. Lake Shore, &c., R. R. Co., 84 N.

Y. 157, 178 (1881); Spear v. Hart, 3 Robertson, 420 (1865); Bright v. Lord, 51 Ind. 272 (1875); City of Ohio v. Cleveland, &c., R. R. Co., 6 Ohio St. 489 (1856); Wright v. Tuckett, 1 Johns. & H. 266 (1860); De Gendre v. Kent, L. R., 4 Eq. 288 (1867).

⁵ Clive v. Clive, Kay, 600 (1854); Black v. Homersham, L. R., 4 Exch. Div. 24 (1878). Cf. Curry v. Woodward, 44 Ala. 305 (1870). In Burroughs v. North Carolina R. R. Co., 67 N. C. 376 (1872), it is held that a sale of shares of stock in a railway company, carries with it the dividends declared by the company, when they are to be paid at a time subsequent to the transfer. In this case it appears that a dividend was declared upon the stock of the North Carolina Railroad Company, on the sixteenth day of February, payable on the first days of April and July following, and that upon the seventeenth day of February, being the day after the dividend was declared, the owner of certain shares transferred them. Under these circumstances it was held that the transferee acquired the dividends as well the stock by his purchase. Browne v. Collins, L. R., 12 Eq. 586 (1871), is to the effect that profits of a partnership accrued and earned before, but not set aside *qua* profits, until after the death of the testator, belongs to the *corpus* of the estate, and that profits accruing after his death go to the tenant for life as income.

⁶ Brundage v. Brundage, 60 N. Y. 544 (1875); affirming s. c. 1 Thomp. & C. 82 (1873); also 65 Barb. 397 (1873).

pro rata, equal and without preference. If the company has issued preferred stock, the holders thereof constitute a class by themselves, and shareholders of that class will be entitled, as a class, to dividends in preference to holders of the common stock. But as between shareholders of the same class there can be no discrimination, and profits set aside for dividends must be evenly divided among the stockholders according to the amount of stock each one owns.¹ Accordingly there can be no lawful discrimination in the division of dividends, although the subscription price of part of the stock is due and unpaid,² nor can there be a discrimination between the large and small stockholders of a company as to the manner of payment of dividends.³ After paying a dividend to a part of the shareholders, the corporation cannot refuse to pay the rest, upon the ground that by so doing, the capital stock will be impaired,⁴ or that all the surplus earnings have been either paid out as dividends, or invested in permanent improvements.⁵

¹ Luling v. Atlantic Mutual Ins. Co., 45 Barb. 510 (1865); Howell v. Chicago, &c., R. R. Co., 51 Id. 378 (1868); Jones v. Terre Haute, &c., R. R. Co., 57 N. Y. 196 (1874); affirming s. c. 29 Barb. 353 (1859); Ryder v. Alton, &c., R. R. Co., 13 Ill. 516 (1851); State v. Baltimore, &c., R. R. Co., 6 Gill, 363 (1847); Atlantic, &c., Telegraph Co. v. Commonwealth, 3 Brewster (Penn.), 366 (1870); Hale v. Republican River Bridge Co., 8 Kan. 466 (1871); Coey v. Belfast, &c., Ry. Co. (Irish Rep.) 2 C. L. 112 (1866); Harrison v. Mexican Ry. Co., L. R., 19 Eq. 358 (1875). Cf. Chase v. Vanderbilt, 62 N. Y. 307 (1875). If the directors of a corporation, in making a distribution of a dividend, omit to apportion a *quota* thereof to certain shares of stock, the owner of those shares can maintain *assumpsit* against the company for breach of the contract, which the law implies from the relationship of the parties, that an equal distribution of dividends will be made. Jackson's Admrs. v. Newark Plankroad Co., 31 N. J. Law, 277 (1865).

² Oakbank Oil Co. v. Crum, L. R., 8 App. Cas. 65 (1882).

³ Accordingly, where a dividend was declared, viz., to all stockholders owning less than fifty shares cash, to all of fifty shares and over, part cash and part in interest-bearing bonds of the corporation, the discrimination was held invalid and

unlawful. State v. Baltimore, &c., R. R. Co., 6 Gill, 363 (1848); Jones v. Terre Haute, &c., R. R. Co., 57 N. Y. 196 (1874). So also where a part of the authorized capital stock remained untaken, and a resolution of the directors was carried into effect, by which the untaken portion of the stock was issued to those shareholders not in arrears upon shares previously taken, to the exclusion, as to the new shares, of those in arrears upon the original issue, in was held an invalid discrimination, and an unlawful imposition of a penalty upon those in arrears. Reese v. Bank of Montgomery County, 31 Penn. St. 78 (1855).

⁴ Stoddard v. Shetucket Foundry Co., 34 Conn. 542 (1868).

⁵ Beers v. Bridgeport Spring Co., 42 Conn. 17 (1875). But where a company, having bought in its own stock, reissued it *pro rata* among the stockholders, and a stockholder, who had between the date of the purchase and the time of the distribution assigned a part of his stock, sued the company for a *pro rata* of the reissued stock, upon the basis of the number held by him at the date of the purchase, it was held that there had been no discrimination against him, and that as to him, the distribution upon the basis of the shares he owned at the time of the reissue was an equitable one. Coleman v. Columbia Oil Co., 51 Penn. St. 74

A bill in equity may be maintained by a stockholder to prevent an unequal or unfair distribution of the profits of the company,¹ and for an injunction to restrain a dividend, when stock has been fraudulently overissued, until a true list of the holders of genuine stock can be obtained.² In New York it is held that closing the books for a time, previous to the payment of a dividend, cannot as to the owner of the stock issued during the interval, deprive him of that dividend.³

§ 545. *A dividend when declared is a debt due absolutely to the shareholder.*—When a dividend out of the earnings of the company has been regularly declared and is due, it becomes immediately the individual property of the shareholder. There is, *eo instante*, a severance, for the use and benefit of the members of the corporation, of so much of the accumulated earnings as are declared, and the dividend thereafter exists as a separate fund, distinct from the capital stock or surplus profits. It then becomes the absolute property of the stockholders.⁴

Accordingly, whenever a dividend is regularly declared and

(1865). *Cf.* *Miller v. Illinois Central R. Co.*, 24 Barb. 312 (1857); *Gray v. Portland Bank*, 3 Mass. 364 (1807).

¹ *Luling v. Atlantic Mutual Ins. Co.*, 45 Barb. 510 (1865). *Cf.* *Harrison v. Mexican Ry. Co.*, L. R., 19 Eq. 358 (1875). In New Jersey it seems that the action might be at law, as for a breach of the contract for an equal distribution which the law implies. *Jackson's Admr. v. Newark Plankroad Co.*, 31 N. J. Law, 277 (1865).

² *Underwood v. New York, &c., R. R. Co.*, 17 How. Prac. 537 (1859), a case growing out of the Schuyler frauds in New York.

³ *Jones v. Terre Haute, &c., R. R. Co.*, 57 N. Y. 196 (1874).

⁴ *Van Dyck v. McQuade*, 86 N. Y. 38 (1881); *Jermain v. Lake Shore, &c., R. R. Co.*, 91 Id. 483 (1883); *Hill v. Newichawanick Co.*, 71 Id. 593 (1877); affirming s. c. 8 Hun, 459 (1876); *Brundage v. Brundage*, 60 N. Y. 544 (1875); affirming s. c. 65 Barb. 397 (1873); *Spear v. Hart*, 3 Robertson, 420 (1865); *Scott v. Central R. R. & Banking Co. of Georgia*, 52 Barb. 45 (1868); *King v. Paterson, &c., R. R. Co.*, 29 N. J. Law, 82, 504 (1860); *Beers v. Bridgeport Spring Co.*, 42 Conn. 17 (1875); *Harris v. San Francisco Sugar Refining Co.*, 41 Cal. 393

(1871); *Fawcett v. Laurie*, 1 Drew. & Sm. 192 (1860); *Hart v. St. Charles St. Ry. Co.*, 30 La. Ann. 758. *Cf.* *Paton v. Sheppard*, 10 Simons, 186 (1839); *Carlisle v. Southeastern Ry. Co.*, 1 Mac. & G. 689 (1850). Where a railway company, being solvent, declared a dividend, and deposited the money to pay it with a firm of bankers, and subsequently withdrew what remained on deposit at the bank,—some of the shareholders not having claimed their dividend,—and then passed into the hands of a receiver, it was held, in an action by one who was a shareholder at the time the dividend was declared, and the deposit thereof made, but who had not drawn his dividend, that the fund deposited at the bank belonged to the shareholders and not to the corporation, and that accordingly the shareholders, each of them, acquired a lien in equity upon the fund, to the extent of the amount to which they were respectively entitled, which followed the fund into the hands of the receiver. It was further held that a stockholder might apply on petition for such a dividend, and that it was not necessary to bring an action therefore. *Matter of Le Blanc*, 14 Hun, 8 (1878); upon the latter point *cf.* *People v. Merchants & Mechanics Bank*, 78 N. Y. 269 (1879).

credited to a depositor, it becomes his property, to which he is entitled in preference to the creditors of the corporation.¹ If, however, the funds to pay a dividend are placed by the corporation on deposit, at a bank or elsewhere, the deposit is made and remains at the risk of the corporation, and not of the shareholders.² But it cannot be withdrawn and reclaimed either by the corporation or a receiver of the corporation, because the shareholders acquire, by virtue of the declaration of the dividend, a lien in equity upon the deposit.³ And the shareholders' right to a dividend, regularly declared, and to the fund set apart by the corporation to pay the dividend, is not affected by the subsequent insolvency of the corporation.⁴ But where no specific fund has been set aside, a shareholder, not having claimed or received his dividend, has, upon the insolvency of the corporation, merely a claim of debt against the corporation and must come in and fare as the other creditors do.⁵ A dividend is something distinct and separable from the fund upon which it is declared, and it may be the subject of assignment by a shareholder before it is received from the corporation.⁶ It becomes a debt when by the terms of the resolution declaring it, it is made payable, and if no time be fixed for payment, then the intent is to be gathered from circumstances.⁷ So it is held that a dividend must be made payable within a reasonable time after it is declared, and when once declared cannot be revoked.⁸ And not only must the time of payment be reasonable, but a reasonable place of payment must be designated, and the entire transaction must be in good faith.⁹

§ 546. *It is a debt which may be collected by legal proceedings.*—The debt which the corporation owes its shareholders,

¹ Van Dyck v. McQuade, 86 N. Y. 38 (1881).

² King v. Paterson, &c., R. R. Co., 29 N. J. Law, 82, 504 (1860).

³ Matter of Le Blanc, 14 Hun, 8 (1878); Beers v. Bridgeport Spring Co., 42 Conn. 17 (1875).

⁴ Le Roy v. Globe Insurance Co., 2 Edw. Chan. 657 (1836).

⁵ Lowne v. American Fire Insurance Co., 6 Paige, 482 (1837).

⁶ Marten v. Gibbon, 33 L. T. (N. S.) 561 (1875). Cf. Jermain v. Lake Shore, &c., R. R. Co., 91 N. Y. 483 (1883). Bargains in prospective dividends are trans-

actions, which, by rule 61 of the Stock Exchange, the committee will not recognize or enforce. The contract is, however, one which is not contrary to law, and it is good between the parties. Marten v. Gibbon, *supra*.

⁷ Brundage v. Brundage, 60 N. Y. 544 (1875); s. c. 65 Barb. 397; City of Ohio v. Cleveland, &c., R. R. Co., 6 Ohio St. 489 (1856). Cf. Burroughs v. North Carolina R. R. Co., 67 N. C. 376 (1872).

⁸ Beers v. Bridgeport Spring Co., Conn. 17 (1875).

⁹ King v. Paterson, &c., R. R. Co., 29 N. J. Law, 82 (1860).

when a dividend is declared and the day of payment arrives, is one which may be collected by the usual action at law. A suit to enforce the declaration of a dividend must be in equity, but when the dividend is not paid after it has been regularly declared, the shareholder's action is at law, and he may sue in *indebitatus assumpsit* for the amount due him according to the terms of the resolution declaring the dividend.¹ It is, however, held that the remedy of an unrecorded transferee to recover a dividend cannot be at law.² It has been held also that a bill in equity will lie to enforce payment of a dividend unjustly withheld.³ But *mandamus* is not a proper remedy in such a case.⁴ A contract of directors to pay a dividend as a debt, at fixed intervals, being in reality a preferred dividend, cannot be enforced either at law or in equity, except out of net profits, like other dividends.⁵ A demand is necessary before the action at law by the shareholder can be maintained,⁶ and a mere letter of inquiry has been held under this rule, an insufficient demand.⁷ A demand while the shares are under and subject to an attachment by the corporation, is not such a demand as this rule contemplates.⁸ The demand must

¹ *Coe v. Belfast, &c., Ry. Co., Irish Rep.*, 2 C. L. 112 (1866); *Jackson's Admr. v. Newark Plankroad Co.*, 31 N. J. Law, 277 (1865); *West Chester, &c., R. R. Co. v. Jackson*, 77 Penn. St. 321 (1875); *King v. Paterson, &c., R. R. Co.*, 29 N. J. Law, 504 (1860); *Keppel's Admr. v. Petersburg R. R. Co., Chase's Dec.* 167 (1868); *Stoddard v. Shetucket Foundry Co.*, 34 Conn. 542 (1868); *City of Ohio v. Cleveland, &c., R. R. Co.*, 6 Ohio St. 489 (1856); *Marine Bank of Baltimore v. Biays*, 4 Har. & J. 338 (1818); *State v. Baltimore, &c., R. R. Co.*, 6 Gill, 363 (1847); *Kane v. Bloodgood*, 7 Johns. Chan. 90 (1823); *Jones v. Terre Haute, &c., R. R. Co.*, 57 N. Y. 196 (1874); *Fawcett v. Laurie*, 1 Drew. & Sm. 192 (1860); *Dalton v. Midland Counties Ry. Co.*, 13 C. B. 474 (1853). *Cf. Stevens v. South Devon Ry. Co.*, 9 Hare, 313 (1851). But if a shareholder is not entitled to share in the dividend according to the terms of the resolution declaring it, he cannot have his action of *assumpsit*. *State v. Baltimore, &c., R. R. Co.*, 6 Gill, 363 (1848). In such a case it seems that his claim against the corporation would be that his rights of membership had been infringed by the inequitable act of the corporate management in declaring the dividend improperly or irreg-

ularly, and in refusing him participation equally and equitably in the profits of the concern.

² *Chambersburgh Ins. Co. v. Smith*, 11 Penn. St. 120 (1849); *Northrup v. Curtis*, 5 Conn. 246 (1824); *Northrup v. Newton, &c., Co.*, 3 Id. 544; *Cleveland, &c., R. R. Co. v. Robbins*, 35 Ohio St. 483 (1880). *Cf. Hall v. Rose Hill, &c., Co.*, 70 Ill. 673 (1873); *Oxford Turnpike Co. v. Bunnell*, 6 Conn. 552 (1827). *Contra, Hill v. Newichawanick Co.*, 48 How. Prac. 427; s. o. aff'd, 71 N. Y. 593 (1877).

³ *Beers v. Bridgeport Spring Co.*, 42 Conn. 17 (1875); *Le Roy v. Globe Insurance Co.*, 2 Edw. Chan. 657 (1836).

⁴ *Van Norman v. Central Car., &c., Co.*, 41 Mich. 166 (1879).

⁵ *Painesville, &c., R. R. Co. v. King*, 17 Ohio St. 534 (1867).

⁶ *Keppel's Admr. v. Petersburg R. R. Co., Chase's Dec.* 167, 213 (1868); *Hagar v. Union National Bank*, 63 Me. 509 (1874); *Scott v. Central R. R. & Banking Co. of Ga.*, 52 Barb. 45 (1868); *State v. Baltimore, &c., R. R. Co.*, 6 Gill, 363 (1847); *King v. Paterson, &c., R. R. Co.*, 29 N. J. Law, 504 (1860).

⁷ *Scott v. Central R. R. & Banking Co. of Ga.*, *supra*.

⁸ *Hagar v. Union National Bank*, *supra*.

have been made at the office of the company, or at least at the place where the dividend is, by the terms of the resolution by which it was declared, made payable.¹ But, with reference to the necessity of this antecedent demand, it is perhaps the better opinion that the commencement of the action is, of itself, a good and sufficient demand, and that, in consequence, no formal demand before bringing the suit is necessary.² Under ordinary circumstances interest is not recoverable upon dividends which have been declared, but which the shareholder has not claimed. The right to interest arises only upon a demand and a refusal to pay.³ But in regard to interest upon dividends on preferred shares, the rule is otherwise. The agreement to pay preferred or guaranteed dividends is usually the principal inducement to take the stock, and in general the dividends promised are the only return for the use of the money advanced. Hence, upon a failure to declare a preferred dividend when one ought to be declared, or when funds which might have been used to pay such a dividend are otherwise employed, there is a misapplication of the corporate resources, and hence, for this the shareholder may have his action, and he may recover the dividend as well as interest thereon.⁴ Interest upon the debt and the Statute of Limitations

¹ See the cases generally in the three preceding notes.

² *Robinson v. National Bank of New Berne*, 95 N. Y. 637 (1884). This accords with the settled theory of the law as to demand in other similar cases. See *East New York, &c., R. R. Co. v. Elmore*, 5 Hun, 214 (1875); *Delamater v. Miller*, 1 Cowen, 75 (1823); *Everett v. Coffin*, 6 Wend. 693 (1831); *Walradt v. Maynard*, 3 Barb. 584 (1848); *Carroll v. Cone*, 40 Barb. 220 (1862); *Ayer v. Ayer*, 16 Pick. 327 (1835).

³ *Boardman v. Lake Shore, &c., R. R. Co.*, 84 N. Y. 157, 187 (1881). *Cf. Adams v. Fort Plain Bank*, 36 N. Y. 255 (1867), where it is held that whenever a debtor is in default, in not paying money pursuant to contract, the creditor is entitled to interest by way of damages.

⁴ *Manning v. Quicksilver Mining Co.*, 24 Hun, 360 (1881); *Prouty v. Michigan Southern, &c., R. R. Co.*, 1 Hun, 655, 667 (1874); *Boardman v. Lake Shore, &c.,*

R. R. Co., 84 N. Y. 157, 188 (1881). In the case last cited the court said: "Having thus misappropriated the funds out of which the interest was to be paid to the preferred stockholders, the company should be compelled to pay interest on the sums which their own act prevented from being paid. They refused to fulfill the contract, or to do what was required by law to pay the plaintiff the dividend to which he was entitled, and compelled him to bring an action to enforce the declaration of dividends, and under these circumstances have no claim to be exempted from the payment of interest as damages, as a consequence of their failure to perform a plain obligation. The plaintiff became damaged by the refusal of the company to declare a dividend when they had funds for that purpose, and by the diversion of such funds his right to interest accrued by being compelled to institute an action to enforce the same." See Ch. XVI.

run only from the date of the demand.¹ The plaintiff, in such an action as this, must be an individual shareholder suing in his own behalf, and one cannot sue for the benefit of all.² And, in general, the corporation itself is the proper defendant, upon the ground that for an illegal refusal to pay a dividend the corporate officers are not to be held personally liable.³ But where the treasurer of an incorporated company withheld a dividend belonging to one of the stockholders, to satisfy a claim of his own against the stockholder, an action of *assumpsit* against him individually was sustained.⁴ And in a case where a stockholder had been unjustly deprived of his stock, it was held that he could not sue an individual shareholder to recover a dividend which should have been paid to him, but that his action was properly against the corporation.⁵ In actions on the part of shareholders to enforce the payment of dividends, the validity or legality of the dividend cannot be questioned by the corporation.⁶ But when a corporation is sued for a dividend by two claimants therefor, it may support a bill of interpleader between them.⁷

§ 547. *Right of the corporation to apply dividends to the payment of debts due to it by the shareholder.*—It is well settled that if, at the time a dividend becomes payable, the stockholder owes the corporation any debt, the dividend due that shareholder may be applied in liquidation of the indebtedness, and if the corporation is sued for the dividend it may set up the debt by way of set-off or counterclaim.⁸ This, however, amounts to a cor-

¹ *State v. Baltimore, &c., R. R. Co.*, 6 Gill, 363 (1847); *Keppel's Admrs. v. Petersburg R. R. Co.*, Chase's Dec. 167, 213 (1868); *Philadelphia, &c., R. R. Co. v. Cowell*, 28 Penn. St. 329 (1857).

² *Carlisle v. Southeastern Ry. Co.*, 2 Hall & Tw. 366 (1850); *Morgan v. Great-eastern Ry. Co.*, 1 Hem. & M. 560 (1863); *Carpenter v. New York, &c., R. R. Co.*, 5 Abb. Prac. 277 (1857).

³ *Smith v. Poor*, 40 Me. 415 (1855); *s. c.* 3 Ware, 148 (1858).

⁴ *Williams v. Fullerton*, 20 Vt. 346 (1848).

⁵ *Peckham v. Van Wagenen*, 83 N. Y. 40 (1880).

⁶ *Stoddard v. Shetucket Foundry Co.*, 34 Conn. 542 (1868).

⁷ *Salisbury Mills v. Townsend*, 109

Mass. 115 (1871). See also § 387. In England the rule was formerly otherwise. *Dalton v. Midland Ry. Co.*, 12 C. B. 458 (1852); *Scott v. Central R. R. & Banking Co. of Ga.*, 52 Barb. 45 (1868). Where a corporation is sued by a stockholder for a dividend declared by the directors and all the other stockholders have received their dividends and retained them, the company cannot be allowed to set up its defense to the suit that the dividend has not been earned, and that its payment would withdraw a part of the capital of the company. *Stoddard v. Shetucket Foundry Co.*, *supra*.

⁸ *Hagar v. Union National Bank*, 63 Me. 509 (1874); *King v. Paterson, &c.*, Ry. Co., 29 N. J. Law, 504 (1860); *Sar-*

porate lien on the stock, so far as dividends are concerned, and it is doubtful whether it should be upheld where the registered stockholder had sold and transferred his certificate of stock before the dividend was declared.

§ 548. *Dividends which impair the capital stock are illegal, and may be recovered back from the stockholders.*—As already shown,¹ a dividend can be lawfully declared only when sufficient net profits have been earned to pay that dividend. Accordingly, a dividend paid wholly or partly from the capital stock is illegal, and subjects the corporation and the shareholders who are parties to it, to serious liability. It is the well determined doctrine of the courts of this country that the capital stock is a trust fund to be jealously preserved intact for the benefit of corporate creditors.² Hence the rule that, where dividends are paid in whole or in part out of the capital stock, corporate creditors, being such when the dividend was declared, or becoming such at any subsequent time, may, to the extent of their claims, compel the shareholders to whom the dividend has been paid, to refund whatever portion of the dividend was taken out of the capital stock.³ In this country shareholders are bound to take notice of

gent v. Franklin Ins. Co., 8 Pick. 90 (1829); Bates v. New York Ins. Co., 3 Johns. Cas. 238 (1802). But in Merchants Bank of Easton v. Shouse, 102 Penn. St. 488 (1883), where a stockholder of the bank died indebted to the bank and insolvent, and after his death the bank went into liquidation, and declared a *pro rata* distribution of its assets to its stockholders, it was held that the bank had no right, either by charter or under the general banking act of 1850, to retain, by way of lien, or set-off, the amount apportionable to the decedent's stock, on account of his indebtedness to the bank, and that his administratrix might recover the amount for administration and distribution to the general creditors of the deceased. *Acc.* Brent v. Bank of Washington, 2 Cranch C. C. 517 (1824). And in *Ex parte* Winsor, 3 Story C. C. 411 (1844), an application of a dividend to the payment of an unpaid call was held illegal. The soundness of this decision may, however, well be questioned.

¹ See § 539, *supra*.

² See § 199, *supra*.

³ Curran v. State of Arkansas, 15

How. 304 (1853); Railroad Company v. Howard, 7 Wall. 392 (1868); Johnson v. Laffin, 5 Dill. 65 note (1878); Wood v. Dummer, 3 Mason, 308 (1824); Gratz v. Read, 4 B. Mon. 178 (1843); Bank of St. Marys v. St. John, 25 Ala. 566 (1854); Bartlett v. Drew, 57 N. Y. 587 (1874); Osgood v. Laytin, 48 Barb. 463 (1867); s. c. 3 Keyes, 521; Heman v. Britton, 5 West. Rep. 330 (Mo. 1886); Rance's Case, L. R. 6 Chan. 104 (1870); Story's Equity Juris. (13th ed., 1886), § 1252. In Lexington Life, &c. Ins. Co. v. Page, 17 B. Mon. 412, (1856), it is held that the action to recover the dividend, in such a case, may be maintained by the directors. The shareholders of a corporation have in Louisiana, no right to appropriate any part of its assets to pay salaries due them as officers of the company, or due them on any other account, until all creditors who are not stockholders, have been paid. Cochran v. Ocean Dry Dock Co., 30 La. Ann. 1365 (1878). *Cf.* Hollister v. Hollister Bank, 2 Abb. App. Dec. 367 (1865); Skrainka v. Allen, 7 Mo. App. 434 (1879); Ward v. Sittingbourne, &c. Ry. Co., L. R. 9 Ch. 488 (1874).

the true character and condition of the capital stock, and they cannot escape liability by reason of their ignorance. Actual notice is not necessary, and if a dividend has been paid out of the capital stock they are conclusively presumed to have known it, and are liable to an action to enforce a repayment. They cannot claim to occupy the position of innocent or *bona fide* holders.¹ But in England the doctrine that the capital stock is a trust fund for the benefit of corporate creditors is not recognized, and both the courts and the legislature proceed, in fixing the liability of shareholders to creditors, upon an entirely different theory from that which obtains in this country. Neither the Winding up Act of 1848 nor the Companies Act of 1862 make any special provision for the protection of the corporate creditors as against the stockholders. And by the courts neither shareholders nor directors are held bound to examine entries in any of the corporate books, and a knowledge of their contents is not imputed to them. The doctrine of constructive notice is not extended so as to impute to shareholders a knowledge of the condition of the corporate finances.² However, upon the theory that a reduction of the capital stock is *ultra vires*, the English courts, where dividends have been paid out of the capital stock, have sustained actions to compel shareholders to whom the dividend was paid, to repay the same to the corporation.³ And when it appears that a dividend declared is likely to be paid out of something else than net profits, such a payment may be enjoined.⁴

In Massachusetts at an early day, there existing no general system of equity jurisdiction in that State, corporate creditors would seem to have been remediless when dividends had been declared and paid to their prejudice out of the capital stock, because it was the rule there that an action at law to compel the shareholders to refund would not lie. *Vose v. Grant*, 15 Mass. 505, 517 (1819); *Spear v. Grant*, 16 Id. 9, 15 (1819). *Cf. Paschall v. Whitsett*, 11 Ala. 472 (1847), to the point that after dissolution of the corporation, a shareholder is not liable to the process of garnishment at the suit of a corporate creditor.

¹ *Peterson v. Illinois Land & Loan Co.*, 6 Bradw. 257 (1880); *Clapp v. Peterson*, 104 Ill. 26 (1882); *Bank of St. Marys v. St. John*, 25 Ala. 566 (1854); *National Trust Co. v. Miller*, 33 N. J. Eq. 155 (1880); *Sagory v. Dubois*, 3 Sandf.

Chan. 466 (1846); *Hastings v. Drew*, 76 N. Y. 9, 19 (1879); *Osgood v. Laytin*, 3 Keyes, 521 (1867); *Gratz v. Redd*, 4 B. Mon. 178 (1843); *Lexington Life, &c. Ins. Co. v. Page*, 17 Id. 412 (1856). See *Main v. Mills*, 6 Biss. 98, and the note (1874). *Cf. Sawyer v. Hoag*, 17 Wall. 610 (1873); *Railroad Co. v. Howard*, 7 Id. 392 (1868); *Curran v. State of Arkansas*, 15 How. 204 (1853); *Wood v. Dummer*, 3 Mason, 308 (1824).

² *In re Denham & Co.*, L. R. 25 Chan. Div. 752 (1883).

³ *Holmes v. Newcastle-upon-Tyne Abattoir Co.*, 45 L. J. Chan. 383 (1875). See also *The Queen v. Liverpool, &c. Ry. Co.*, 21 L. J. (Q. B.) 284 (1852).

⁴ *McDougall v. Jersey Imperial Hotel Co.*, 2 Hem. & M. 528 (1864). But see *Ward v. Sittingbourne, &c. Ry. Co.*, L. R. 9 Chan. 488 (1874).

§ 549. *Proceedings to recover back such a dividend.*—It is, in general, the practice where dividends have been paid out of the capital stock, in prejudice of the rights of corporate creditors, for a judgment-creditor, upon the return of his common law execution against the corporation wholly or partly unsatisfied, to commence an action in equity on behalf of himself and all other creditors who may come in, in the nature of a creditor's bill, against the stockholders, to whom the dividend was unlawfully paid, to recover back so much thereof as was paid out of the capital stock.¹ In such a suit the private property of the shareholder may be reached to satisfy the claim of a creditor of the corporation, at least to the extent that the dividend received by that stockholder impaired the capital stock of the corporation.² It is a necessary condition precedent to the right to bring this action, that a valid judgment shall have been obtained against the corporation, and that execution thereon shall have been returned wholly or partly unsatisfied, and this judgment is conclusive as to the merits of the creditor's claim.³ In New York the receiver of an insolvent corporation may maintain an action for the benefit of the creditors against the shareholders to recover the sums received by them as dividends at the time the company was insolvent, and in such an action the creditors of the corporation are proper parties, for the purpose of restraining them from proceeding individually against the shareholders separately to recover the unlawful dividends.⁴ But a receiver's suit cannot in such a case be brought for the benefit of the stockholders.⁵ The corporate creditors cannot call upon the shareholders to account for dividends made in good faith, in the regular order of business, when the concern was prosperous and before the distribution of its property, although the corpora-

¹ *Hastings v. Drew*, 76 N. Y. 9 (1879); *Bartlett v. Drew*, 57 N. Y. 587 (1874); *Osgood v. Laytin*, 48 Barb. 463; s. c. 3 Keyes, 521 (1867); *McLean v. Eastman*, 21 Hun, 312 (1880); *Bank of St. Marys v. St. John*, 25 Ala. 566 (1854); *Taylor v. Miami Exporting Co.*, 5 Ohio, 162 (1831); *Gratz v. Redd*, 4 B. Mon. 178 (1848); *Curran v. State of Arkansas*, 15 How. 304 (1853); *Rance's Case*, L. R. 6 Chan. 104 (1870). Cf. *Brewer v. Michigan Salt Association*, 58 Mich. 351 (1885). And see *Vose v. Grant*, 15 Mass. 505,

517 (1819); *Spear v. Grant*, 16 Id. 9, 15 (1819).

² *Bartholomew v. Bentley*, 15 Ohio, 659 (1846).

³ *Sturges v. Vanderbilt*, 78 N. Y. 384 (1878); *Hastings v. Drew*, 76 Id. 9 (1879). See *Brewer v. Michigan Salt Association*, 58 Mich. 351 (1885).

⁴ *Osgood v. Laytin*, 5 Keyes, 521 (1867). See also *Lexington Life, &c. Ins. Co. v. Page*, 17 B. Mon. 412 (1856).

⁵ *Butterworth v. O'Brien*, 39 Barb. 192 (1863); s. c. 24 How. Prac. 438. Cf. *McLean v. Eastman*, 21 Hun, 312 (1880).

tion subsequently becomes insolvent and is dissolved.¹ In the creditor's suit all the stockholders who can be reached, should be made parties defendant, and as to those unknown, or insolvent, or beyond the jurisdiction, there should be a proper averment in the bill.² The corporation also should be made a party defendant to the bill.³ The shareholder, who is compelled to pay more than his equitable proportion of any unpaid corporate debt may, in a proper proceeding, resort to his associates for contribution.⁴ And a transferee of stock against which creditors have this claim, takes it subject to its proportional share of the burden, and may be held liable to respond in a creditor's suit, in the same way and to the same extent as his transferrer.⁵ The Statute of Limitations runs in favor of shareholders who receive such dividends in good faith and without actual notice, from the time they are declared, as against the corporation and its creditors.⁶

§ 550. *The liability herein of the corporate officers.*—The liability of the corporate officers as to dividends paid out of the capital stock is not definitely determined. That they are liable for the amount of any such dividend that they themselves receive as shareholders cannot, perhaps, be questioned.⁷ Many cases go to the full extent of holding the directors liable absolutely for all dividends paid out of capital stock. But it may be stated as the more discriminating rule that when, in the absence of a statutory accountability, the directors act in good faith and there is no imputation of negligence on their part, they are not to be charged

¹ Reid v. Eatonton Manfg. Co., 40 Ga. 98 (1869).

² Wood v. Dummer, 3 Mason, 308 (1824); Bartlett v. Drew, 57 N. Y. 587 (1874). In the case last cited—a leading authority in New York—it is held that the creditor is not required to bring his suit on behalf of other creditors who may choose to come in, but may sue alone and for his own benefit exclusively, and that he need not make all the stockholders parties, but may pursue one, any, or all as he may elect, upon the theory that with the equities between the stockholders themselves he has nothing to do unless he choose to intervene to settle them. Cf. Pacific R. R. Co. v. Cutting, Jr., 27 Fed. Rep. 638 (1886); Williams v. Boice, 38 N. J. Eq. 364 (1885).

³ First National Bank of Hannibal v. Smith, 6 Fed. Rep. 215 (1879), followed

in Dormitzer v. Illinois, &c. Bridge Co., 6 Fed. Rep. 217 (1881).

⁴ Bartlett v. Drew, *supra*.

⁵ Hastings v. Drew, 76 N. Y. 9, 18 (1879); *Contra*, Hurlbut v. Taylor, 62 Wis. 607 (1885).

⁶ Lexington Life, &c. Ins. Co. v. Page, 17 B. Mon. 412 (1856). Cf. Scott v. Eagle Fire Ins. Co., 7 Paige, 198 (1838); DePeyster v. American Fire Ins. Co., 6 Id. 486.

⁷ Main v. Mills, 6 Biss. 98, and the note (1874); Rance's Case, L. R. 6 Chan. 104 (1870). But see, apparently *contra*, *In re Denham & Co.*, L. R. 25 Chan. Div. 752 (1883), wherein both officers and members of a corporation were absolved from liability to refund a dividend which had been paid in good faith, although in fact it impaired the capital stock.

merely because the dividend they authorize impairs the capital stock.¹ But where the directors willfully and knowingly declare and pay a dividend out of the capital stock, they are personally liable to refund that dividend.² Frequently also when a dividend is paid out of the capital stock, the directors are made liable therefor by statute without reference to any fraud or fraudulent intent on their part.³ In Kentucky it is doubted whether directors are liable to creditors, the courts of that State seeming to incline to hold them liable only to the corporation or the stockholders.⁴ While in Massachusetts the liability of the directors in these cases has been held enforceable by corporate creditors only.⁵ In England the directors are not liable to the shareholders as a body, upon a bill in equity, but where the directors have fraudulently misrepresented the affairs of the company, and paid dividends

¹ *Excelsior Petroleum Co. v. Lacey*, 63 N. Y. 422 (1875). *Cf. Gillett v. Moody*, 3 N. Y. 479 (1850). In *Stringer's Case*, L. R. 4 Chan. 475 (1869), it was held, in accordance with this view, that where the action of a board of directors in making a dividend was *bona fide*, they are not liable for errors of judgment in preparing a balance sheet showing the assets of the concern. In this case it appears that the directors included among the corporate assets a debt due the company by the Government of the Confederate States; some cotton owned by the company but stored within the limits of the Confederacy, and certain merchant ships engaged in running the blockade, all which were estimated at their full value. These assets being subsequently destroyed and lost to the company, its bankruptcy followed. *Cf. Reid v. Eatonton Manfg. Co.*, 40 Ga. 98 (1869); *Scott v. Central R. R. & Banking Co. of Georgia*, 52 Barb. 45 (1868); *Keppel's Admrs. v. Petersburg R. R. Co.*, Chase's Dec. 167 (1868).

² *Gratz v. Redd*, 4 B. Mon. 178, 194 (1843); *Hill v. Frazier*, 22 Penn. St. 320 (1853); *In re Alexandra Palace Co.* L. R. 21 Chan. Div. 149 (1882); *Salisbury v. Metropolitan Ry. Co.*, 22 L. T. (N. S.) 839 (1870); *Flitcroft's Case*, L. R. 21 Chan. Div. 519 (1882); *Evans v. Coventry*, 8 De G., M. & G. 835 (1857); *Tarquand v. Marshall*, L. R. 4 Chan. 376 (1869). In *Burnes v. Pennell*, 2 House of Lords Cases, 497, 531 (1849), Lord Brougham, said: "I beg to be understood as going with those who view with

the greatest severity the conduct of railway directors in declaring dividends which can only be paid out of capital, because I consider that that is, of itself, a most vicious and fraudulent course of conduct. It is telling the world that their profits are large, when it may be that their profits are *nil*, or that their losses are large, with no profits. It is a false and fraudulent representation by act and deed, much to be reprobated, and I go to the full length of what my noble and learned friend has laid down, that it would be a just ground, if a course of conduct of this sort were pursued, coupled with such circumstances as clearly to show a fraudulent intent, for proceedings of a graver nature against these parties."

³ In Massachusetts, officers of a corporation can be charged, under the statute in force upon the subject in that State [Stat. 1862, chap. 218, § 3; Stat. 1870, chap. 224, §§ 40, 42], with corporate debts after a judgment against the corporation, and after a demand and return upon the execution. *Chamberlin v. Huguenot Manufacturing Co.*, 118 Mass. 532, 536 (1875); *Priest v. Essex Manufacturing Co.*, 115 Id. 380 (1874). So in New Jersey, directors are similarly liable by statute. *Rev. of N. J.* (1877), p. 178; *Williams v. Boice*, 38 N. J. Eq. 364 (1885). And in New York, 1 *Rev. Stat.* chap. XVIII, tit. 2, art. 1, §§ 1, 10.

⁴ *Lexington, &c. R. R. Co. v. Bridges*, 7 B. Mon. 556, 559 (1847).

⁵ *Smith v. Hurd*, 12 Metc. 371 (1847), and the cases in note 3, *supra*.

when none were earned, each shareholder has his remedy at law against the directors.¹ Under certain circumstances, in the absence of actual fraud, the directors who have been compelled to pay the claims of corporate creditors, may, in turn, recover what they have paid, in an action against the shareholders.² But a director from whom a recovery is had under the Pennsylvania statute,³ as a wrong-doer, has no right of subrogation as against the corporation.⁴ And claims against directors who are made liable by statute in these cases may, in the absence of actual fraud on their part, be barred by laches.⁵

¹ *Turquand v. Marshall*, L. R. 4 Chan. 376 (1869). Cf. *Lexington, &c. R. R. Co. v. Bridges*, 7 B. Mon. 556, 559 (1847).

² *Salisbury v. Metropolitan Ry. Co.*, 22 L. T. (N. S.) 839 (1870). *In re Alexandra Palace Co.*, L. R. 21 Chan. Div. 149 (1882).

³ Act of 7th April, 1849, § 9.

⁴ *Hill v. Frazier*, 22 Penn. St. 320

(1853). In this case it was held that in the creditor's suit against the director, the corporation itself is not a necessary co-defendant.

⁵ *In re Mammoth Copperopolis of Utah*, 50 L. J. Chan. 11 (1880). This is a decision construing § 165 of the Companies Act of 1862. See also *Williams v. Boice*, 38 N. J. Eq. 364 (1885).

CHAPTER XXXIII.

LIFE-ESTATES AND REMAINDERS IN SHARES OF STOCK.

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| <p>§ 551. Questions arising herein.</p> <p>552. Cash dividends belong to the life-tenant.</p> <p>553. Stock or property dividends.</p> <p>554. (a.) The Pennsylvania rule.</p> <p>555. (b.) The Massachusetts rule.</p> <p>556. (c.) The English rule.</p> | <p>§ 557. The intent of the creator of the trust.</p> <p>558. The apportionment of dividends.</p> <p>559. The right to subscribe for new shares, as between life-tenant and remainderman.</p> <p>560. Miscellaneous incidents herein.</p> |
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§ 551. *Questions arising herein.*—It is well settled that shares of stock may be the subject of a legacy, gift, sale, or trust.¹ It frequently happens that the stock passes to the purchaser, legatee, or donee, not absolutely and as an entirety, but divided into two estates—a life-estate, and a remainder over. Important questions then may arise as to the respective rights and duties of the owners of the two estates. These questions sometimes involve the right of custody and similar other incidental rights. But the difficulty which has involved the courts in far the greater perplexity, is the question to whom, as between life-tenant and remainderman, do the dividends belong. Upon this subject the courts have not been able to agree upon a uniform rule. In general, a dividend declared during the existence of the particular estate, being strictly income, belongs to the tenant for life. But whenever an unusually large or extraordinary dividend is declared, whether it is to be paid in money or in stock, the interests of the life-tenant and remainderman conflict, and very considerable difficulty has been experienced in finding a satisfactory solution of the problems that have arisen.

§ 552. *Cash dividends belong to the life-tenant.*—In the case of an ordinary cash dividend there is, in general, very little difficulty. By an ordinary or regular cash dividend is meant one which is declared at regular intervals, in the ordinary course of

¹ Perry on Trusts (3d ed.), §§ 544, (2d ed.) § 465; Angell & Ames on Corp. 545, and the notes; Morawetz on Corp. (11th ed.) § 557, note a.

business, by the corporation, the receipt of which is, under ordinary circumstances, looked forward to by the stockholders as a natural incident of their ownership. Such dividends are, according to the settled rule, income, and so many of them as are declared during the continuance of the life-estate go to the life-tenant.¹ With respect to these dividends it is not, as a rule, material when they were earned. Dividends declared during the existence of the particular estate belong to the tenant for life, even though they are not, by their terms, payable until after his death. But dividends declared before the life tenancy begins, even though they are payable after the commencement thereof, do not belong to the tenant for life, but go to the *corpus* of the estate. The life-tenant is entitled to only such dividends as are declared during the lifetime of his estate.² This rule applies, even though it may be shown that the dividend in question was earned, wholly or in part, before the commencement of the life-estate,³ or that the amount of it is unusually or extraordinarily large.⁴

§ 553. *Stock or property dividends.*—When a stock or property dividend is declared upon shares held in trust, or owned in such a way that one person has an estate therein for life, and an-

¹ *Barclay v. Wainwright*, 14 Ves. 66 (1807); *Norris v. Harrison*, 2 Madd. 268 (1817); *Clive v. Clive*, Kay, 600 (1854); *Murray v. Glassey*, 17 Jur. 816 (1853); *Preston v. Melville*, 16 Sim. 163 (1848); *Cuming v. Boswell*, 2 Jur. (N. S.) 1005 (1856). This is by all the authorities assumed to be a rule beyond dispute. See the cases generally cited hereafter, and *cf.* *Ware v. McCandlish*, 11 Leigh (Va.), 595 (1841).

² *De Gendre v. Kent*, L. R. 4 Eq. 283 (1867). The facts in this case aptly illustrate the rule declared in the text. Dividends were declared in June, 1865, and made payable July 15, 1865, and January 15, 1866. The stock from which the dividends arose was bequeathed to A for life, with remainder over to B. The testatrix died December 31, 1865, and it was held as to the January dividend that it belonged to the estate and not to the life-tenant, upon the ground that it had not been declared during the existence of the life-estate. *Cf.* *Browne v. Collins*, L. R. 12 Eq. 586, 594; *Locke v. Venables*, 27 Beav. 598 (1859). See also *Cogswell v. Cogswell*, 2 Edw. Chan. 231 (1834);

Abercrombie v. Riddle, 3 Md. Chan. 320 (1850); *Wright v. Tuckett*, 1 Johns. & Hem. 266 (1860); *Furley v. Hydés*, 42 L. J. Chan. 626. But in Massachusetts it has been held that sometimes dividends declared after the life-tenant's death will, nevertheless, go to his estate. Thus, a life tenancy in stock for the support of the testator's widow and children was held to entitle the widow's estate to a dividend declared after her death, but for a period which expired before that event. *Johnson v. Bridgewater Manfg. Co.*, 14 Gray, 274 (1859). See also *Ellis v. Proprietors of Essex Merrimack Bridge*, 2 Pick. 243 (1824); *Gifford v. Thompson*, 115 Mass. 478 (1874).

³ *Richardson v. Richardson*, 75 Me. 570 (1884); s. c., 4 Am. Prob. Rep. 352; *Bates v. Mackinley*, 31 Beav. 280 (1862); *Jones v. Ogle*, L. R. 8 Chan. 192 (1872); *Goldsmith v. Swift*, 25 Hun, 201 (1881); *Jermain v. Lake Shore, &c.*, R. R. Co., 91 N. Y. 483 (1883).

⁴ *Price v. Anderson*, 15 Sim. 473 (1847); *Barclay v. Wainwright*, 14 Ves. 66 (1807); *Witt v. Steere*, 13 Id. 263 (1807).

other person the remainder over, there at once arises a contest between life-tenant and remainderman. Their interests necessarily conflict, because, if such a dividend is held to be income, it belongs to the tenant for life; whereas, if it is held to be a part of the *corpus*, or principal, it inures to the benefit of the remainderman's estate. We find three well-defined rules upon this subject, which may be denominated respectively the Pennsylvania, the Massachusetts, and the English rule. They lead to essentially contrary conclusions, and will be considered in order.

§ 554. (a.) *The Pennsylvania rule.*—This rule, inasmuch as it obtains in every State in the Union, excepting Georgia and Massachusetts, might well be called the American rule. It proceeds upon the theory that the court, in disposing of stock or property dividends, as between life-tenant and remainderman, may properly inquire as to the time when the fund out of which the extraordinary dividend is to be paid was earned or accumulated. If it is found to have accrued or been earned before the life-estate arose, it is held to be principal and to belong to the *corpus* of the estate, and not to go to the life-tenant, without reference to the time when it is declared or made payable. In this way it inures to the benefit of the remainderman's estate. But when it is found that the fund out of which the dividend is paid, accrued, or was earned, not before but after the life-estate arose, then it is held that the dividend is income, and belongs to the tenant for life.¹ This salutary rule prevails not only in Pennsyl-

¹ This rule was first declared in *Earp's Appeal*, 28 Penn. St. 368 (1857). In this case it appears that, by the will of Robert Earp, the appellants were entitled to receive during their lives the "rent, income, and interest" of 540 shares in the Lehigh Crane Iron Works. At the testator's death, in 1848, a surplus had accumulated out of the regular profits of the business which increased the value of the stock at that time from \$50 per share, the sum originally paid for it, to \$125 per share. This surplus continued to increase until 1854, when it was converted into new stock, and a stock dividend declared. By this proceeding the number of shares in the hands of the trustee was increased from 540 to 1350, and the value per share, after the issue of new stock, was about \$80. "It thus appears," say the court, "that, at the time of the death of Robert

Earp, the 540 shares of stock then held were worth over \$67,500, and that at the time the new certificates were issued for 1350 shares, the latter were worth \$108,000. The difference, \$40,500, is the amount of profits arising since the death of the testator. The profits arising since the death of the testator are 'income,' within the meaning of the will, and should be distributed among the appellants. These profits amounted at the time of the issue of the new certificates of stock to \$40,000, exclusive of the current semi-annual dividends which had previously been declared and paid. That sum is the rightful property of the appellants. The managers might withhold the distribution of it for a time for reasons beneficial to the interests of the parties entitled. But they could not, by any form of procedure whatever, deprive the owners of it and give it

vania, where it seems to have first been clearly declared,¹ but also in many other jurisdictions.²

to others not entitled. The omission to distribute it semi-annually, as it accumulated, makes no change in its ownership. . . . Standing upon principle, and upon the intention of the testator, as plainly expressed in his will, we have no difficulty whatever in making this disposition of the fund."

In *Wiltbank's Appeal*, 64 Penn. St. 256 (1870), the facts were that the testator bequeathed his residuary estate in trust for life with remainder over. This *residuum* included 300 \$25 shares of the stock of the New Hampshire Gas Company, and 20 \$100 shares of the stock of the New Hampshire Ry. Co. Subsequently to the testator's death the railroad company increased its stock, selling the new shares to its stockholders at \$75 per share, and the gas company did the same, selling its shares at par. The trustees did not take the new shares, but sold the privilege of subscribing for them, and the court held that the proceeds of the sale were income of the trust and belonged to the life-tenant. See also the following later Pennsylvania cases in point: *Moss's Appeal*, 83 Penn. St. 264 (1877); *Biddle's Appeal*, 99 Id. 278 (1882); s. c., 3 Am. Prob. Rep. 442; *Vinton's Appeal*, 99 Penn. St. 434 (1882); s. c., 3 Am. Prob. Rep. 231; *In re Thompson's Estate*, 11 Week. Notes Cas. 482 (1882). *Of Robert's Appeal*, 92 Penn. St. 407 (1880); *Thomson's Appeal*, 89 Id. 36 (1879).

¹ *Vide* preceding notes.

² So in New Jersey. *Van Doren v. Olden*, 19 N. J. Eq. 176 (1868); *Ashhurst v. Field's Admr.*, 26 Id. 1 (1875). In the former case, where shares of stock were held in trust for life, and an extra stock dividend was declared by the corporation, the new shares being sold to the shareholders at fifty per cent. of their face value, it was held that, so far as the fund from which the stock dividend was made had been accumulated before the testator's death, the shares taken by the trustees went to augment the *corpus* of the trust, and that the rest was income belonging to the life-tenant. This seems to be exactly the Pennsylvania rule. The court, in that case, say: "Where trust funds, of which the income, interest, or profits are given to one person for life, and the principal bequeathed over upon the death of the life-tenant, are invested,

either by the trustee or at the death of the testator, in stock or shares of an incorporated company, the value of which consists in part of an accumulated surplus or undivided earnings laid up by the company, as is frequently the case, such additional value is part of the capital; this, as well as the par value of the shares, must be kept by the trustees intact for the benefit of the remainderman, but the earnings of such capital, as well as upon the par value of the shares, belongs to the life-tenant."

Van Doren v. Olden, supra.

New Hampshire—*Lord v. Brooks*, 52 N. H. 72 (1872). Here it appeared that the plaintiff, in 1839, as trustee under the marriage settlement of Mrs. Brooks, held forty shares in the P. Bank. The charter of this bank expired in 1845, and the liquidator paid to the trustee the \$4,000 of capital invested, and \$1,260 out of the surplus. The trustee employed the fund to buy fifty-three shares in the P. Exchange Bank, which in turn dissolved in 1864, paying to the trustee, in capital and surplus, something over \$8,000. Of this sum the trustee invested \$4,000 in forty shares of the First National Bank of P. Mrs. Brooks died in 1869, at which time the forty National Bank shares were worth more than the forty shares of the P. Bank at the time of the creation of the trust in 1839. The balance not invested in 1864 in bank shares was claimed by the remainderman and also by the administrator of Mrs. Brooks, and the court held that this balance clearly belonged to the administrator as income of the trust upon the ground that net earnings remain the property of the corporation until a dividend is declared, but that, while it is often advisable to reserve earnings, their character is not changed by the delay in distributing them, and that when the necessity or propriety of reserving them ceases, and the reserve is divided, the question whether it is income or capital will depend on its origin, it being income if originally derived from net earnings. In *Wheeler v. Perry*, 18 N. H. 307 (1846), a testator left in trust for life with remainder over two shares of the par value of \$500 each, worth, however, \$1,500 each to the testator's knowledge at the date of the will. Subsequently the corporation dissolved, and paid to its shareholders

In New York the Court of Appeals has not been called upon to consider this question.¹ But it has frequently arisen in the lower courts, and there the rule, as announced by the courts of Pennsylvania, has been strenuously insisted upon.² The principle upon which this class of cases proceed is that the *corpus* of the trust must not on the one hand be impaired by the declaration of a dividend, and that, on the other hand, it must not be augmented at the expense of the life-estate; that the life-tenant is entitled to all the increase or earnings of the fund when declared as dividends; that the trustee must maintain intact the value of the *corpus* as it existed at the time of the creation of the trust, apportioning dividends if necessary between life-estate and remainder to that end, but that whatever the trust fund earns during the

\$1,525 on each share. It was held that these dividends were of capital, and went wholly to the *corpus* of the estate. See also *Peirce v. Burroughs*, 58 N. H. 302 (1878).

Maine—*Richardson v. Richardson*, 75 Maine, 570 (1884); s. c., 4 Am. Prob. Rep. 352. In this case the court, in deciding that a cash dividend of fifty per cent. belonged to the life-tenant, intimated strongly that it would not have reached a contrary conclusion if the dividend had been paid in stock instead of money, it appearing that it was made out of profits, and said: "Although the dividend amounts to fifty per cent. on the capital shares, our opinion is that it and all the dividends made or to be made like it must be paid to the life-tenant. If in this she is fortunate to-day, she may have been exceedingly less so in the past, and no one can anticipate what may come of the morrow. The declaration of this dividend is a confession by the company that her previous annual income has, from the caution of its officers, been too small, and is now made up to her. The present atones for the past."

¹ "The right to stock dividends as between tenant for life and remainderman, has not been considered by the court of last resort in this State." *Riggs v. Cragg*, 89 N. Y. 479, 487 (1882), by Andrews, C. J.

² In *Riggs v. Cragg*, 26 Hun, 89, 103 (1881), it was decided by Daniels, J., that in New York, stock dividends created by and declared from the surplus earnings of a company are as between a tenant for life and those interested in the remainder,

to be treated as income and not as an addition to the capital, but where the fund from which the stock dividend is declared has been created, not by the earnings of the company but by a sale of a portion of its real estate, the rule is otherwise. It is true that this case was reversed on appeal, but the reversal was upon another point. See the preceding note. In the earliest case in which this question came before the Supreme Court—*Clarkson v. Clarkson*, 18 Barb. 646 (1855)—it was held that a stock dividend of sixty per cent. belonged to the life-tenant, where it appeared that such a disposition of it would not impair the capital of the trust fund, left by will to be invested in shares, "the interest, dividends, and proceeds" to be paid to A for life, with remainder over to B. This case was followed in *Simpson v. Moore*, 30 Barb. 637 (1859); *Estate of Woodruff*, 1 Tucker (New York Surrogate Ct.), 58 (1865), and *Goldsmith v. Swift*, 25 Hun, 201 (1881). *Cf. Cragg v. Riggs*, 5 Redf. 82 (1880); *Scovil v. Roosevelt*, 5 Id. 121 (1881). Profits upon the sale of stock are principal and not income in New York. *Whitney v. Phoenix*, 4 Redf. 180 (1880). In *Hyatt v. Allen*, 56 N. Y. 553, 557 (1874), the Court of Appeals intimated plainly its disapproval of the rule prevailing in England upon this subject, and a review of all the reported cases possibly indicates that when the question shall come before the court of last resort in this State it will not reverse what has already been established in the inferior courts. *Cf. Farwell v. Tweddle*, 10 Abb. N. C. 94.

continuance of the life-estate, whether it be paid in cash dividends or stock dividends, is to go to the tenant for life. Accordingly a trust fund, under the operation of this rule, will be neither increased nor diminished by the declaration of dividends during the continuance of the life-estate; dividends from surplus earnings accumulated during the life-tenant's time will go to him as income, and dividends from surplus earnings accumulated before his estate commenced, will remain as principal in the hand of the trustee. The court will therefore go behind the mere formal declaration of the dividend to investigate the matter, and will apportion the dividend, if it be necessary, between life-tenant and remainderman, preserving the *corpus* intact, and paying the increase to the owner of the particular estate.

§ 555 (b.) *The Massachusetts rule.*—This rule, which prevails only in Massachusetts and Georgia, is sometimes called “the rule in *Minot's Case*.” It regards cash dividends, whether large or small, as income, and stock dividends, whenever earned and however declared, as capital, and the rule accordingly is a simple one. Cash dividends belong to the tenant for life and stock dividends to the *corpus*.¹ It is argued in defense of this theory that

¹ *Minot v. Paine*, 99 Mass. 101 (1868). In this case the principle is thus stated: “A simple rule is to regard cash dividends, however large, as income, and stock dividends, however made, as capital.” In subsequent cases this rule has been affirmed and elaborated. *Daland v. Williams*, 101 Mass. 571 (1869); *Leland v. Hayden*, 102 Id. 542 (1869); *Heard v. Eldridge*, 109 Id. 258 (1872); *Rand v. Hubbell*, 115 Id. 461 (1874); *Gifford v. Thompson*, 115 Id. 478 (1874); *Hemenway v. Hemenway*, 134 Id. 446 (1883); s. c. 3 Am. Prob. Rep. 429; *New England Trust Co. v. Eaton*, 140 Mass. 532 (1886); s. c. 4 Am. Prob. Rep. 368. While the rule in the text was, as has been shown, first declared in *Minot v. Paige, supra*, there was a tendency toward it in the earlier cases. In *Harvard College v. Amory*, 9 Pick. 446 (1830), the earliest case in which the question seems to have come before the Massachusetts court, it appears that funds left in trust for life with remainder over to Harvard College, were by the trustees invested in the shares of an insurance company and a manufacturing company. The insurance

company declared an extra dividend of fourteen per cent. from money received under a Spanish treaty in satisfaction of spoliation claims pending at the time of the investment; the manufacturing company declared an extra dividend from the proceeds of the sale of patent rights and machinery, which facts were known at the time of the investment. The court held that extraordinary dividends of this character were not a distribution of capital stocks, but of profits, and were therefore properly set off to the life-tenant. The next case is *Balch v. Hallet*, 10 Gray, 402 (1858), where shares of stock in a wharf and building company were held in trust for life with remainder over. Dividends were declared from the proceeds of the sale of land, &c., and it was held that these were not extraordinary dividends, and that, if they did not impair the *corpus*, they must go as income to the *cestui que trust*. Cf. *Atkins v. Albree*, 94 Mass. 359 (1866). The case of *Minot v. Paige, supra*, is next in chronological order. The opinion in that case, wherein the Massachusetts rule upon this subject was first formulated, deals simply with distribu-

money in the hands of the directors, while it is income to the corporation is not income to the stockholders until a dividend is declared, and that when the corporation invests it in permanent improvements or additions to the corporate property, or expends it in increasing the corporate capacity to do business, it never becomes income to the stockholder, but is an accretion to the capital, and that this is equally so whether the directors elect to increase the number of the shares, or the par value of the shares, or leave the shares unaltered; that if the number of the shares be increased merely for the purpose of facilitating speculation it is an increase of capital stock and not of income; that it is within the proper power of the directors either to withhold dividends and accumulate a surplus to be expended as they deem best,¹ subject only to the interference of a court of equity in case of a gross abuse of powers,² or to pay out the earnings as dividends; that every shareholder takes his stock with knowledge of this fact, and subject to the exercise of this power by the directors, and that when dividends are declared it is practically unwise for the courts to go behind the action of the corporate management and attempt to ascertain how they came by the funds out of which either cost or stock dividends are declared.³ The court may, however, in deciding whether, in a given case, the distribution is a stock or a cash dividend, consider the actual and substantial character of the transaction, and not its nominal character merely.⁴

tions made from *accumulated earnings*. This is in fact the only matter in dispute between life-tenant and remainderman, for it has never been questioned that distributions of the original capital, on the one hand, go to the *corpus*, or to the remainderman—except possibly in the case of certain peculiar corporations, like the Boston Water Power Company, whose regular and only means of making dividends are derived from the sales of their property (*Reed v. Head*, 6 Allen, 174 1863),—while dividends of current earnings, on the other hand, go to the tenant for life.

¹ *Rand v. Hubbell*, 115 Mass. 461 (1874); *In re Barton's Trust*, L. R. 5 Eq. 238 (1868); *Gibbons v. Mahon*, 4 Mackey, 130 (1885); s. c. 54 Am. Rep. 262.

² *Pratt v. Pratt*, 33 Conn. 446 (1866); *Scott v. Eagle Fire Ins. Co.*, 7 Paige, 198, 203 (1838).

³ *Chapman, C. J.*, in *Minot v. Paine* 99 Mass. 101 (1868).

⁴ Thus in *Daland v. Williams*, 101 Mass. 571 (1869), the court, in applying "the rule in *Minot's Case*," where the directors, having voted to increase the capital stock by 3,000 shares, declared a cash dividend of forty per cent., and authorized the treasurer to receive that dividend in payment for 2,800 of the shares, the remaining 200 shares to be sold, held that the transaction was virtually a stock dividend and that the shares must go to the remainderman's fund. *Cf. Rand v. Hubbell*, 115 Mass. 461 (1874). In *Leland v. Hayden*, 102 Mass. 542 (1869), where it appeared that the company had invested its surplus earnings in its own stock, and subsequently declared a dividend of that stock, the life-tenant was held absolutely entitled to it. And again, in *Heard v. Eldridge*, 109 Mass.

This rule has not in general found favor outside of Massachusetts; it has been very severely criticised as unjust and unreasonable.¹ It has not been followed except in Georgia, where the principle underlying the rule is incorporated into the Civil Code,² and possibly by the Supreme Court of the District of Columbia.³

258 (1872), the facts were that a fund held in trust for life consisted of shares in a wharf company whose corporate property consisted of real estate, and its income of rents and wharfage. The city of Boston condemned and took part of its property for public purposes, paying therefore \$185,000, of which the directors distributed \$75,000 among its shareholders, reserving the rest. This was held to be clearly a division of part of the capital stock, which should go to the *corpus*, and not to the income of the trust. *Cf.* with this case, *Balch v. Hallett*, 10 Gray, 402 (1858); *Reed v. Head*, 6 Allen, 174 (1863); *Harvard College v. Amory*, 9 Pick. 446 (1830). In *Gifford v. Thompson*, 115 Mass. 478 (1874), where shares of stock in a railway were held in trust for life, and the railway dissolved, sold its property and declared a dividend of one hundred and fifty per cent., fifty per cent. thereof being undivided earnings, the court held that the undivided earnings were part of the capital represented by the certificates of shares, and that consequently no part of the dividend was income, but that the whole would go to the *corpus* of the trust. *Cf.* *Hemenway v. Hemenway*, 134 Mass. 446 (1883); s. c. 3 Am. Prob. Rep. 429. In *New England Trust Co. v. Eaton*, 140 Mass. 532; s. c. 4 Am. Prob. Rep. 368 (1886), it was held, in an elaborate opinion by Devens, J., that the gain or loss arising from the sale of stock held in trust is the gain or loss of the *corpus*, and that the sum received constitutes a new principal. Accordingly a trustee who has invested in bonds at a premium may retain annually from the income payable to the life-tenant, such sums as will restore to the fund at its maturity what was taken therefrom at the time of the investment. See also the dissenting opinion of Mr. Justice Holmes in this case, and *cf.* *Bowker v. Pierce*, 130 Mass. 262 (1881); *Dodd v. Winship*, 133 Id. 359 (1882); *Wright v. White*, 136 Id. 470 (1884); *Parsons v. Winslow*, 16 Id. 361 (1820); *Lovell v. Minot*, 20 Pick. 116 (1838).

¹ See three interesting and valuable little pamphlets, by a layman, wherein

the merits of the question are fully and learnedly discussed, published by G. P. Putnam's Son, New York, and entitled respectively "Common Sense *versus* Judicial Legislation," "Stock Dividends, the Rule in Minot's Case Restated, with Variations by the Supreme Judicial Court of Massachusetts," and "A Third Chapter on the Rule in Minot's Case." See 5 Am. Law Rev. 720 (July, 1871); Perry on Trusts (3d edition), §§ 544, 545, and the notes.

² The language of the Code is as follows: "The natural increase of the property belongs to the tenant for life, any extraordinary accumulation of the *corpus*, such as issue of new stock upon the shares of an incorporated or joint-stock company attaches to the *corpus*, and goes with it to the remainderman." Code of Georgia, § 2256. In *Millen v. Guerrard*, 67 Ga. 284 (1881); s. c. 44 Am. Rep. 720, the persons having an estate in remainder in certain railway shares, held in trust for life, claimed from the trustee as part of the *corpus* of the trust fund, an extra dividend declared after the testator's death, in certificates of indebtedness payable in ten years or later with interest, from the accumulated earnings of past years, during which no dividends were declared. The court held that, under § 2256 of the Code, the whole of this dividend, however large, went as income to the life-tenant; that, although it was unusually large, it should, because the earnings of previous years had for prudential reasons been withheld, be regarded as "natural increase," and not an "extraordinary accumulation of the *corpus*."

³ *Gibbons v. Mahon*, 4 Mackey, 130 (1885); s. c. 54 Am. Rep. 262. Here a will left shares in trust, to pay dividends to the testator's child for life, "without diminution of the principal." The court held, without citing any authorities, that the life-tenant could not take a stock dividend, when the company having accumulated a surplus, equal in amount to its original capital, issued additional stock after the testator's death, to the amount of this surplus, thereby doubling the capital, and divided it among the stock-

In Rhode Island, however, the courts have adopted a rule somewhat like "the rule in *Minot's Case*," without the modification engrafted upon it by the subsequent decisions of the Massachusetts courts. It is a rule which in general prefers the remainderman to the life-tenant.¹

§ 556. (c.) *The English rule*—In England, the courts have based their rule upon the rather vague distinction between regular or ordinary, and extra or extraordinary dividends,² holding that "regular" dividends, even if increased in amount beyond what is usual, belong as income to the life-tenant, and that "extra" dividends, whether they are paid in cash or stock, belong to the *corpus* of the trust.³ This rule may be said to have had its origin

holders in proportion to the amount originally held by them. It does not very clearly appear in the opinion, whether this surplus was earned wholly or in part, before or after the testator's death, and the reasoning by which the court reaches its conclusion is not satisfactory, but it seems to indicate an attempt to follow the rule in *Minot v. Paine*, 99 Mass. 101, *supra*.

¹ Thus in *Parker v. Mason*, 8 R. I. 427 (1867), when this question first came before the court of last resort in that State, where bank shares were held in trust for life, the directors, fearing that the capital stock had been impaired by some bad debts, reduced the par value of the shares from \$50 to \$25, but, this fear ultimately proving to have been groundless, they issued one new share as a dividend upon each old one, and this the court very properly held to be a mere replacement of the capital which should go to the *corpus*. In *Busbee v. Freeman*, 11 R. I. 149 (1875), it was held that new shares issued to the stockholders, whether gratis or for cash, would go to the remainderman of shares held in trust, because by such an issue the *corpus* of the trust fund would otherwise be impaired, the value of the old shares being reduced to the extent of the new issue. In the latest case that has been handed down in that court, *Petition of Brown*, 14 R. I. 371 (1884); s. c. 51 Am. Rep. 397, it is held that new shares, made out of corporate earnings, and distributed among the stockholders, are not income, and do not go to the life-tenants. In this case, *Minot v. Paine* is followed expressly, and the court, after announcing the rule of that case at length, declares as "entire-

ly inconsistent with this view," the later Massachusetts cases wherein the rigor of the rule is abated, as well as in the case of *Parker v. Mason*, *supra*.

² The courts perhaps uniformly insist upon this distinction, extraordinary dividends may be either of cash or stock, and appear under a variety of names, such as "participations," "distributions," or, more commonly, "bonuses." See *Witts v. Steere*, 13 Vesey, 363 (1807); *Norris v. Harrison*, 2 Madd. 268 (1817); *Hooper v. Rossiter*, McClelland, 527 (1824); *Bates v. MacKinley*, 31 Beav. 280 (1862).

³ To the point that regular dividends, though increased in amount, go as income to the owner of the life-estate, see *Barclay v. Wainwright*, 14 Vesey, 66 (1807); *Price v. Anderson*, 15 Sim. 473 (1847). There is no question that regular dividends, ordinary in amount, go to the life-tenant. See § 552, *supra*. All the authorities assume this as unquestioned. To the point that "extra" or unusual dividends, whether of cash or shares, go to augment the principal of the trust fund, see *Irving v. Houstoun*, 4 Paton's H. of L. Cases, 521, 1803 (a stock dividend); *Hooper v. Rossiter*, McClelland, 527, 1824 (a stock dividend); *In re Barton's Trust*, L. R., 5 Eq. 238, 1868 (a stock dividend); *Paris v. Paris*, 10 Vesey, 185, 1804 (a cash dividend); *Clayton v. Gresham*, 10 Vesey, 288, 1804 (a cash dividend); *Witts v. Steere*, 13 Vesey, 363, 1807 (a cash dividend); *Price v. Anderson*, 15 Sim. 473, 1847 (a cash dividend); *Bates v. MacKinley*, 31 Beav. 280, 1862 (a cash dividend). Cf. *Gill v. Burley*, 22 Beav. 619 (1856); *Straker v. Wilson*, L. R., 6 Chan. 503.

in the opinion of Lord Chancellor Loughborough, in the leading case of *Brander v. Brander*,¹ and in the concurring opinions of Lord Eldon, in the several subsequent cases.² This rule, it will be perceived, rejects both the distinction between stock dividends and cash dividends, upon which the rule in Massachusetts is founded, and also the distinction between distributions of earnings accumulated after the commencement of the life tenancy, and those accumulated before that period, upon which the Pennsylvania rule rests. The English courts have with essential uniformity adhered to it. After some intermediate vacillation,³

¹ 4 Vesey, 800, 801 (1799). In this case a life-tenant held Bank of England shares under a will. The bank having subscribed £1,000,000 to a government loan, and receiving therefor £1,125,000 of annuities, which it resolved to distribute among its stockholders, it was held, in the High Court of Chancery, that this was not income for the life-tenant, but an accretion to the *corpus*.

² The first of these cases is *Paris v. Paris*, 10 Vesey, 185 (1804), where a testator, who died previous to the year 1798, left the dividends on his bank stock to his wife for life, with remainder over. In September, 1804, the bank declared a regular three and one-half per cent. dividend of interest and profits for the preceding half year, and soon after resolved on a division of money at the rate of five pounds per cent. This the life-tenant claimed as a dividend, attempting to distinguish the case of *Brander v. Brander*, *supra*, on the ground that this bonus was probably paid from profits accruing since the testator's death, because three similar dividends had previously been paid; and upon the further ground that the former case was a distribution of stock, and this one of money. But the Lord Chancellor held that the bonus went to the *corpus*, as an extraordinary dividend. It is interesting to note that, in the opinion in this case, the court pointedly disapproved of both the rules which have subsequently grown up in the United States. With respect to what we now call the Pennsylvania rule, Lord Eldon, referring to the case of *Irving v. Houstoun*, 4 Paton's H. of L. Cases, 521 (1803), which had just been handed down in the House of Lords, and in which a distribution of stock by the Bank of Scotland had been held to accrue as principal to the trust fund, said: "The decision

having been made in the House of Lords, the only ground of distinction in this case is, that there is great probability, perhaps moral certainty, that these profits were made during the time of the tenant for life. *But that will not do*; for it comes to this, that in every case in which inquiry can determine that the tenant for life ought to have them, they ought to go according to that inquiry; and that was much considered in the House of Lords." And, with reference to what is known in this country as the "rule in *Minot's Case*," he said, immediately following what has just been quoted: "As to the distinction between stock and money, *that is too thin*, and if the law is that this extraordinary profit if given in the shape of stock, shall be considered capital, it must be capital if given as money. It would be too dangerous to distinguish this case upon these distinctions." *Acc. Cases, temp. Eldon*, cited in the preceding notes.

³ In *Preston v. Milville*, 16 Sim. 163 (1848), the tenant for life was held entitled to a "bonus" of one per cent. in addition to the regular dividend. This seems to have been the result of a misinterpretation of the decisions in *Barclay v. Wainwright*, 14 Vesey, 66 (1807), which was cited by Counsel. In *Murray v. Glasse*, 17 Jur. 816 (1852), the life-tenant was said to be entitled to "bonuses if they were made from profits." In *Plumbe v. Neild*, 6 Jur. (N. S.) 529 (1860), bonuses were given to the tenant for life, on the ground that they were clearly declared "from the profits of the last half year." In *Johnson v. Johnson*, 15 Jur. 714 (1850), it seems that the corporation passed a resolution "that a bonus or increased dividend of £10 per share be added to the usual dividend of £3 per share," and the court, taking probably the ground that

which is, however, more an apparent than a real departure from, or relaxation of the rule declared at the commencement of the controversy between life-tenant and remainderman concerning dividends,¹ the courts of that country have taken what may be believed to be a final stand upon the question, which is fully in accord with what the Chancellor established in *Brander v. Brander*, and *Paris v. Paris*, and which is here set out as the English rule.²

§ 557. *The intent of the creator of the trust.*—It is a familiar rule of construction that in every case the intention of the testa-

it might, in construing the words of the resolution, regard what was distributed *either* as a bonus or a dividend, held it an "increased dividend," and gave it to the tenant for life. Lord Eldon's opinion in *Barclay v. Wainewright*, 14 Vesey, 66 (1807), has sometimes been misunderstood, and that case is cited as "shaking the authority" of the earlier leading cases. So, for example, in *Clarkson v. Clarkson*, 18 Barb. 646 (1855); *Minot v. Paine*, 99 Mass. 101 (1868); *Earp's Appeal*, 28 Penn. St. 368 (1857), but this, it is respectfully submitted, is an entire misconception of what the case decided. The question involved was the disposal of a semi-annual dividend of the Bank of England, which was larger than usual by two per cent. This the court gave to the life-tenant as an increased regular dividend in precise consistency with the established rule. See also *Witts v. Steere*, 13 Vesey, 363 (1807), where the facts were similar, except that instead of increasing the regular dividend, the bank issued an "extra dividend" of five per cent.

This was disposed of by Lord Eldon in strict accord with the rule. In the opinion it is said: "The ordinary dividend proceeds as usual. The question is how this bonus of £5 per cent. out of the interest and profits is to be considered, whether as part of the capital or to go to the tenant for life. It is not for me to say how this would be, if it were *res nova*. The only principle upon which it can stand is the principle that seems to have governed the House of Lords in the case of *Irving v. Houstoun*, that whatever conduct or language the bank may hold, if they do not increase the dividend, but take this mode of distributing the profit, it is part of the capital, and does not belong

to the tenant for life. The bank may so conduct themselves as to avoid the question altogether, for they may increase the dividend, and that increased dividend would be the ordinary fruit of the stock. But if they do not take that course, the manner in which they give the bonus cannot make a difference. Though they may express it differently, the thing is in fact the same."

¹ See the preceding note.

² *In re Barton's Trust*, L. R., 5 Eq. 238 (1868). In this case one was entitled to receive for life the "interest, dividends, shares of profits, or annual proceeds" of certain stock, and the directors, having paid out a portion of the net profits for a fixed period as ordinary cash dividends, retained and applied the remainder of profit to the purchase of new property, and issued new shares to represent what had been so expended. *Wood, V. C.*, in holding that these new shares belonged to the *corpus*, and not to the life-tenant, said: "The dividend to which a life-tenant is entitled, is the dividend which the company chooses to declare. And when the company meet and say that they will not declare a dividend, but will carry over some part of the half years' earnings to the capital account, and turn it into capital, it is competent for them to do so; and where this is done everybody is bound by it, and the life-tenant of those shares cannot complain." *Acc. Bates v. MacKinley*, 31 Beav. 280 (1862). See also *In re Hopkin's Trust*, L. R., 18 Eq. 696 (1874); *Sproule v. Bouch*, L. R., 29 Chan. Div. 635 (1885) [a case in which it was held that the rule will not apply when it appears that the testator intended otherwise]. *Lock v. Venables*, 27 Beav. 598 (1859); *Scholefield v. Redfern*, 32 L. J. Chan. 627 (1863).

tor or of the grantor of the trust deed is the pole star, and that, as far as it can be ascertained, it shall control in the administration of the trust.¹ So also the court will take into consideration in determining the question, as between life-tenant and remainderman, the whole character of the transaction, and the nature and source of the property distributed, with due regard to all the facts preceding, attending, and resulting from the declaration of the dividend.² In general it seems to have been the tendency of the earlier English cases to favor the remainderman, but in the later cases the tendency is even more marked to favor the life-tenant.³ Accordingly it is a settled rule that merely calling a dividend a bonus or a bonus a dividend, will not conclude the court from looking into the facts, and from reaching its conclusions without reference to the mere names applied to the fund distributed.⁴ Accordingly, where it is shown that dividends have been fraudulently retained, in prejudice of the rights

¹ *In re Bouch*, L. R., 29 Chan. Div. 635 (1885); *In re Hopkin's Trusts*, L. R., 18 Eq. 696 (1874); *Jones v. Ogle*, L. R., 14 Eq. 419 (1872); *Re Box's Trusts*, 9 L. T. (N. S.) 372 (1863). *Cf. Read v. Head*, 6 Allen, 174 (1863); *Clarkson v. Clarkson*, 18 Barb. 646 (1855); *Millen v. Guerrard*, 67 Ga. 284 (1881); *Thomson's Appeal*, 89 Penn. St. 36 (1879).

² *Deland v. Williams*, 101 Mass. 571 (1869); *Leland v. Hayden*, 102 Id. 542 (1869); *Rand v. Hubbell*, 115 Id. 461 (1874). In *Minot v. Paine*, 99 Mass. 101 (1868), the rule was laid down that the form in which the dividend was declared should determine to whom it should go. This position is qualified by the subsequent cases. So in *Heard v. Eldridge*, 109 Mass. 258 (1872), it is said: "The suggestion that the intention of the directors shall determine the question whether the dividend is capital or income cannot be correct. . . . It is more safe to look at the character of the property and the transaction." See also *Hartley v. Allen*, 4 Jur. (N. S.) 500, and the cases in the preceding note. Upon this theory, as it seems, it was held in *Lock v. Venables*, 27 Beav. 598 (1859), that a specific bequest of "the dividends, interest, and proceeds" of shares will not pass a bonus on the shares. In *Alcock v. Sloper*, 2 Mylne & K. 699 (1833), the "income of the testator's long annuities" was given to the life-tenant. *Acc. Wilday v. Sandys*, L. R., 7 Eq. 455 (1869). In *Lane v. Lough-*

ran, 7 Vict. L. R. Eq. 19 (1881), it was held that the premium on a lease of part of a trust estate belonged to the tenant for life and not to the *corpus*. An executor may plainly transfer the stock to pay the decedent's debts, although it is bequeathed for life with remainder over. *Franklin v. Bank of England*, 1 Russ. 575 (1826). In *Sproule v. Bouch*, L. R., 29 Chan. Div. 635 (1885), a bonus was held to belong to the tenant for life, it appearing that such was the intention of the parties. *Cf. Bostock v. Blakeney*, 2 Brown's Chan. 653 (1788); *Re Willoughby*, 53 Law Times Rep. 926 (1886); 2 *Perry on Trusts*, §§ 544, 545; *Mr. Moak's note*, 31 Eng. Rep. 328, 332.

³ This may be seen by comparing the opinions in the cases of *Brander v. Brander*, 4 Vesey, 800, 801 (1799); *Bostock v. Blakeney*, 2 Brown's Chan. 653 (1788), and *Paris v. Paris*, 10 Vesey, 185 (1804), with those in the comparatively recent cases of *In re Bouch*, L. R., 29 Chan. Div. 635 (1885); *In re Hopkin's Trusts*, L. R., 18 Eq. 696 (1874), and *Plumbe v. Neild*, 6 Jur. (N. S.) 529 (1860).

⁴ *Hallis v. Allan*, 12 Jur. (N. S.) 638 (1866); *Johnson v. Johnson*, 15 Jur. 714 (1850); *Plumbe v. Neild*, 6 Jur. (N. S.) 529 (1860); *Sproule v. Bouch*, L. R., 29 Chan. Div. 635 (1885); *Hooper v. Rossiter*, 13 Price, 774 (1824); *Millen v. Guerrard*, 67 Ga. 284 (1881); *Daland v. Williams*, 101 Mass. 571 (1869); *Rand v. Hubbell*, 115 Id. 461 (1874).

of the life-tenant, and subsequently a bonus is paid upon the shares, it belongs, as income deferred, to the tenant for life, even though it be called a bonus.¹

§ 558. *The apportionment of dividends.*—When a life-tenant dies before the date at which a dividend is regularly declared, the question arises whether the dividend declared next after his death, for the period of time partially covered by the life-estate, ought or ought not to be apportioned between the reversioner or remainderman and the estate of the life-tenant. It is, in general, the rule in such a case, in the absence of a statutory provision to the contrary, that the dividend is not apportionable, but belongs entirely to the *corpus* of the trust fund.² But where a tenant for life dies on the day a dividend becomes due, his estate will be entitled to the whole of that dividend.³ In England, however, under the statute known as the Apportionment Act of 1870,⁴ dividends are apportionable in these cases between the estate of the life-tenant and the *corpus*,⁵ and in this country, at common law, in one or two jurisdictions, there is a tendency to hold that dividends are apportionable.⁶

¹ *Maclaren v. Stainton*, L. R. 11 Eq. 382; s. c. 3 De G., F. & J. 202 (1861); reversing s. c. 27 Beav. 460 (1859); *Edmondson v. Crosthwaite*, 34 Beav. 30 (1864); *Dale v. Hayes*, 40 L. J. Chan. 244 (1871); s. c. 24 L. T. (N. S.) 12; 19 W. R. 299. *Cf. Lean v. Lean*, 32 L. T. (N. S.) 305; s. c. 23 W. R. 484; *Lambert v. Lambert*, 29 L. T. (N. S.) 878; s. c. 22 W. R. 359; *In re Tinkler*, 45 L. J. (Chan. Div.) 135.

² *Pearly v. Smith*, 3 Atk. 260 (1745); *Sherrard v. Sherrard*, Id. 502 (1747); *Wilson v. Harman*, 2 Vesey, Sen. 672 (1755); *Hartley v. Allen*, 4 Jur. (N. S.) 500 (1858); *In re Maxwell's Trusts*, 1 Hem. & M. 610 (1863); *Scholefield v. Redfern*, 2 Drew. & Sm. 173 (1863); *Foote*, Appellant, 22 Pick. 299 (1839); *Granger v. Bassett*, 98 Mass. 462 (1868); *Clapp v. Astor*, 2 Edw. Chan. 379 (1834). *Cf. Hyatt v. Allen*, 56 N. Y. 553 (1874); *Brundage v. Brundage*, 60 Id. 544, 551 (1875); *Perry on Trusts*, § 556; 1 Williams on Executors, § 836, note m.

³ *Paton v. Sheppard*, 10 Sim. 186 (1839).

⁴ 33 & 34 Vict., chap. 35, § 2.

⁵ This statute provides that "all rents, annuities, dividends, and other periodical payments in the nature of income shall,

like interest on money lent, be considered as accruing from day to day, and shall be apportionable in respect of time accordingly." The courts construe this statute so as to make dividends apportionable between life-tenant and remainderman. *Pollock v. Pollock*, L. R., 18 Eq. 329 (1874), qualifying or explaining *Whitehead v. Whitehead*, L. R., 16 Eq. 528 (1873); *Beavan v. Beavan*, 53 L. T. Rep. 245 (1885). *Cf. Capron v. Capron*, L. R., 17 Eq. 288 (1874). And see *Banner v. Lowe*, 13 Ves. 135 (1806); *Hay v. Palmer*, 2 P. Wms. 501 (1727). The statute applies only to dividends upon the stock of corporations strictly speaking, and not to those upon the shares in private trading corporations. *Jones v. Ogle*, L. R., 8 Chan. 192 (1872). And does not apply to stock dividends. *Hartley v. Allen*, 4 Jur. N. S. 500 (1858).

⁶ In *Ex parte*, Rutledge, 1 Harper's Eq. (S. C.) 65 (1824); s. c. 14 Am. Dec. 696, a dividend was apportioned between life-tenant and remainderman. This is regarded a leading lease in favor of apportionment. In Pennsylvania the interest on municipal bonds, and the bonds of private corporations, is apportionable, but *quere* whether or not the interest on government bonds would be.

§ 559. *The right to subscribe for new shares, as between life-tenant and remainderman.*—The right to subscribe for new shares at par upon an increase of the capital stock, which is an incident of the ownership of the stock, does not belong as a privilege to the life-tenant, but such an increment must be treated as capital, and be added to the trust fund for the benefit of the remainderman. This is equally the rule whether the trustee subscribes for the new stock for the benefit of the trust or sells the right to subscribe for a valuable consideration, in either event the increase goes to the *corpus*.¹ The subsequent income, however, of such increase belongs, as of course, during the continuance of the life tenancy, to the life-tenant as income proper, the new shares are part of the *corpus*, and the life-tenant being entitled to the income from the *corpus*, takes the income from the accretions thereto.²

§ 560. *Miscellaneous incidents herein.*—The life-tenant must pay calls which are made³ and taxes levied,⁴ during the contin-

Wilson's Appeal, 108 Penn. St. 344 (1885); overruling Earp's Will, 1 Parson's Eq. Cas. 553. But in Massachusetts the statute of apportionment is held not to apply to dividends, upon the stock of corporations. *Granger v. Bassett*, 98 Mass. 362, 469 (1868), construing Genl. Stat. of Mass. chap. 97, § 24. In New York an apportionment is provided for by Laws of 1875, ch. 542.

¹ *Atkins v. Albree*, 94 Mass. 359 (1866); *Brinley v. Grou*, 50 Conn. 66 (1882); s. c. 4 Am. Prob. Rep. 324; *Biddle's Appeal*, 99 Penn. St. 278 (1882); s. c. 3 Am. Prob. Rep. 442; *Moss's Appeal*, 83 Penn. St. 264 (1877); *Vinton's Appeal*, 99 Penn. St. 434 (1882); s. c. 3 Am. Prob. Rep. 231; *Goldsmith v. Swift*, 25 Hun, 201 (1881); *Sanders v. Bromley*, 55 L. T. (N. S.) Chan. Div. 145 (1886). Profit upon the sale of stock is *corpus* and not income for the life-tenant. *Whitney v. Phoenix*, 4 Redf. (N. Y. Surro.) 180 (1880). Cf. *Leitch v. Wells*, 48 N. Y. 585 (1872). In *Hemenway v. Hemenway*, 134 Mass. 446 (1883); s. c. 3 Am. Prob. Rep. 429, where a testator bequeathed a fund to trustees, with a discretion to sell certain of the securities, and substitute other investments, paying the "net rents and income" to one for life, remainder over, and the trustees with the proceeds of certain bonds worth more than par which fell due after the testator's death, had

bought other bonds at par and at par and accrued interest, it was held that the life-tenants, as against the remainderman, were entitled to all the net income on the bonds owned by the testator or bought by the trustees at a premium, and that sums paid for accrued interest should be repaid from interest subsequently received. *Acc. New England Trust Co. v. Eaton*, 140 Mass. 532 (1886); s. c. 4 Am. Prob. Rep. 368. Sometimes certificates of new stock are not stock dividends. *Chicago, &c., R. R. Co. v. Page*, 1 Biss. 461 (1864). In *Londesborough v. Somerville*, 19 Beav. 295 (1854), where consols were sold just before a dividend day, and the proceeds invested in realty, a tenant for life was held entitled to be paid, as income on the consols, the difference between the price obtained and the value exclusive of the next dividend.

² *Moss's Appeal*, 83 Penn. St. 264 (1877); *Biddle's Appeal*, 99 Penn. St. 278 (1882); s. c. 3 Am. Prob. Rep. 442, and the cases generally cited in the preceding note. *In re Bromley*, 55 L. T. (N. S. Chan. Div.) 145 (1886).

³ *Re Box's Trusts*, 9 L. T. (N. S.) 372 (1863).

⁴ *Webb v. Town of Burlington*, 28 Vt. 188 (1856); *Citizens' Mutual Ins. Co. v. Lott*, 45 Ala. 185 (1871). Cf. *Nat. Albany Exchange Bank v. Wells*, 18 Blatchf. 478 (1880).

uance of his estate, upon shares held in trust for his benefit. And where stock to produce a fixed income is bequeathed for life, a subsequent increase in the earnings from that stock inures to the benefit of the life-tenant.¹ But the enhanced price for which stock sells by reason of dividends earned but not declared, belongs entirely to the remainder.² A life-tenant is not entitled to have the stock transferred to him on the corporate books.³ But the corporation, if it had notice of the trust, may be held liable for transferring shares in prejudice of the rights of the life-tenant.⁴ And an administrator who permits an irregular transfer in fraud of the life-tenant's rights, makes himself personally liable.⁵

¹ *Russell v. Loring*, 3 Allen, 121 (1861). In this case stock to produce \$2,000 of income per annum subsequently produced considerably more per annum than that sum. This excess was held to belong to the life-estate. But when a fixed income is bequeathed and the income fails, or falls short, the principal must be resorted to. *Bonham v. Bonham*, 33 N. J. Eq. 476; *Haydel v. Hurck*, 72 Mo. 253. The opposite rule, however, prevails in New York. *Delaney v. Van Aulen*, 84 N. Y. 16 (1881); reversing s. c. 21 Hun, 274. *Cf. Crawford v. Dox*, 5 Hun, 507 (1875.)

² *Scholefield v. Redfern*, 32 L. J. Chan. 627 (1863); *Abercrombie v. Riddle*, 3 Md. Chan. 320 (1850); *Van Blarcom v. Daget*, 31 N. J. Eq. 783. *Cf. Lonsborough v. Somerville*, 19 Beav. 295 (1854); *Matter of Stutzer*, 26 Hun, 481 (1882).

³ *Collier v. Collier*, 3 Ohio St. 369 (1854). *Cf. State v. Robinson*, 57 Md. 486.

⁴ *Stewart v. Fireman's Ins. Co.*, 53 Md. 564 (1880).

⁵ *Keeney v. Globe Mill Co.*, 39 Conn. 145 (1872). See also *Ames v. Williamson*, 17 West Va. 673.

CHAPTER XXXIV.

TAXATION OF SHARES OF STOCK.

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| <p>§ 561. The four methods of taxing corporate interests.</p> <p>562. Rights of the stockholders in regard to the first three methods of taxation.</p> <p>563. Tax on shares of stock as distinguished from the other methods.</p> <p>564. Tax on stockholders residing in the State creating the corporation.</p> <p>565. Tax on resident stockholders in a non-resident or foreign corporation.</p> <p>566. Tax on non-resident stockholders</p> | <p>in resident or domestic corporation.</p> <p>§ 567. Double taxation.</p> <p>568. Exemptions from taxation as affecting tax on shares of stock.</p> <p>569. Taxation of national bank stock.</p> <p>570. Place in which shares in national bank stock may be taxed.</p> <p>571. The tax must not be greater than that imposed on other "moneyed capital."</p> <p>572. The bank may bring suit to restrain illegal tax on its stockholders.</p> |
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§ 561. *The four methods of taxing corporate interests.*—There are, in general, four methods of taxing corporate interests. These are, first, by a tax on the franchise; second, on the capital stock; third, on the real estate and personal property of the corporation; fourth, by a tax on the shares of stock in the hands of the stockholders.¹ There is another mode of taxation which is sometimes adopted—a tax on corporate dividends; but since this is generally construed to be only a method of valuing the franchise or capital stock, it can hardly be called a fifth method of taxing corporate interests.² It is entirely within the discretion of the legislature to say which one of these four methods of taxation shall be adopted, where the matter is not regulated by the State Constitution. Not only this, but it is also within the discretion

¹ Redfield on Railways, vol. II, 3d ed., p. 453, says: "We here find the clear recognition of three kinds of corporate property taxable to the corporation, and the shares in the hands of the corporators distinctly defined as a fourth species of corporate property, which is taxable only to the owner or holders—1. The capital stock; 2. The corporate property; 3. The franchise of the corporation. All of which is taxable to the corporation; and the shares in the capital stock, which is taxable only to the share-

holders." See also Id. 5th ed. 423. In the case *Ottawa Glass Co. v. McCaleb*, 81 Ill. 556 (1876), the court said: "A corporation is possessed of three kinds of property subject to taxation—first, the capital stock; second, the corporate property; and third, the franchise; and the shares may be assessed against their owners." See also *Louisville, &c., R. R. Co. v. State*, 8 Heisk. (Tenn.) 663, 795.

² See *State of O. v. Franklin Bk.*, 10 O. 91 (1840); *People v. Home Ins. Co.*, 92 N. Y. 328 (1883).

of the legislature to tax the corporation in two or more of these ways, to levy a double tax on the corporate interests, and even to levy a treble or quadruple tax thereon.

§ 562. *Rights of the stockholders in regard to the first three methods of taxation.*—The stockholders in a corporation have very little to do directly with any of the first three modes of taxing corporate interests. The tax is levied directly against the corporation, and is paid by the corporate officers out of the treasury of the corporation. If the tax is unauthorized or illegal, or improperly assessed, or is based on too high a valuation, it is ordinarily the duty of the corporate officers to rectify or oppose such tax. The stockholders have nothing to do with the ordinary transaction of corporate business, of which this forms a part. Where, however, the corporate officers refuse, upon request of one or more stockholders, to oppose or decline to pay an unauthorized tax, levied in any one of the three methods mentioned above, the stockholder himself may bring a suit in a court of equity, in behalf of and for the protection of the corporate interests, to enjoin the payment and collection of such unauthorized tax.¹

§ 563. *Tax on shares of stock as distinguished from the other methods.*—A tax on shares of stock is clearly different from a tax upon the franchise, the corporate property, or the capital stock.²

¹ Dodge v. Woolsey, 18 How. 331 (1855); State Bk. of O. v. Knoop, 16 Id. 369 (1853); Wilmington R. R. Co. v. Reed, 13 Wall. 264 (1871); Delaware R. R. Tax, 18 Id. 206 (1873); Greenwood v. Freight Co., 105 U. S. 13 (1881); Paine v. Wright, 6 McClell, 395 (1855); Foote v. Linck, 5 McClell, 616 (1853), holding also that the corporation is a necessary party, and that if the complainant is a non-resident he may bring the suit in the United States Circuit Court. Bailey v. Atlantic, &c., R. R. Co., 5 Dill. 22 (1874); Paruley v. R. R. Cos., 5 Dill. 13 and 25 (1874). But the stockholder must allege actual tender of the amount of tax conceded to be due. Allegation of readiness to pay is insufficient. Huntington v. Palmer, 8 Fed. Rep. 449 (1881). See also Trask v. Maguire, 18 Wall. 391 (1873); Wood v. Draper, 24 Barb. 187 (1857); London v. City of Wilmington, 78 N. C.

190 (1878). The case of State v. Flavell, 24 N. J. L. 370 (1854), denies this right, and says: "It is objected, and rightfully, on the part of the defendants, that it does not lie in the mouth of every individual stockholder, whether his interest be small or great in a corporation aggregate, to complain of an illegal assessment against the body corporate. The exception should be made by the corporation itself which is wrongfully assessed, and not by the individual stockholders."

² Judge Cooley, in his learned work on Taxation, 2d ed., 231, clearly recognizes this principle of law when he says: "A tax on the shares of stockholders in a corporation is a different thing from a tax on the corporation itself or its stock, and may be laid irrespective of any taxation of the corporation where no contract relations forbid." Citing cases.

Especially is it important to distinguish a tax on shares of stock from a tax on the capital stock.¹ The latter is always taxed against the corporation, is paid by the corporation, and is based on a valuation which does not necessarily depend on the value of the shares of stock. A tax on the shares of stock is generally levied directly against the stockholders themselves at their place of residence, is based on the market value of the stock, and is entirely distinct from the location, interests, property, or taxes of the corporation itself. There are, however, some instances of taxation herein which are on the border line between the two. Thus a statute expressly laying a tax on the shares of stock, but requiring the corporation to pay that tax from the corporate funds, has been held in Iowa to be a tax, not on the shares of stock, but on the capital stock. In other jurisdictions it has been held to be a tax on the shares of stock. A tax laid on shares owned by non-residents of the State which creates the corporation and which levies the tax, is a tax on the shares of stock and not on the capital

¹ In the case *Porter v. Rockford, R. I., &c., R. R. Co.*, 76 Ill. 561 (1875), the court clearly recognized this distinction, and said: "The legal property of the shareholder is quite distinct from that of the corporation, although the shares of stock have no value save that which they derive from the corporate property and franchise, and a tax levied upon the property of the one is not, in a legal sense, levied upon the property of the other. See also *Bradley v. Bauder*, 36 O. St. 28 (1880). Cf. *Delaware R. R. Tax*, 18 Wall. 206, 230 (1873); *Farrington v. Tennessee*, 95 U. S. 679, where the distinction is clearly drawn; *Quincy Bridge Co. v. Adams Co.*, 88 Ill. 615 (1878). In the case *North Ward National Bank v. City of Newark*, 39 N. J. L. 380 (1877), the court said: "The moneyed capital of a bank is an entirely different thing from its capital stock. The former is the property of the corporation. It may consist of cash or of bills discounted, or be in part invested in real estate or in the securities of the Federal government. In whatever form it is invested, it is owned by the bank as a corporate entity and not by the stockholders. The stock or shares represent the interests of the shareholders, which entitle them to participate in the net profits of the bank in the employment of its capital, and is a distinct and independent interest or property in the shareholders, held by them like other

property." The case of *Porter v. Rockford, &c., R. R. Co.*, *supra*, holds also that a tax on the "capital stock" means the property of the corporation and not the aggregate of the shares of stock. See also *State v. Hamilton*, 5 Ind. 310 (1854), where the word "stock" was construed to mean the tangible property of the corporation. But see *Trask v. Maguire*, 18 Wall. 391 (1873). And even though the value of the capital stock is estimated by the aggregate value of the shares, it is still a tax on the capital stock. *New O., &c., R. R. Co. v. Bd. of Assessors*, 32 La. Ann. 19 (1880). See also *State Bank of Va. v. City of Richmond*, 79 Va. 113. So also where the franchise is valued in that manner for taxation. *Commonwealth v. Hamilton Mfg. Co.*, 94 Mass. 298 (1866); *Atty.-Gen. v. Bay State Min. Co.*, 99 Mass. 148 (1868). *Hamilton Co. v. Massachusetts*, 6 Wall. 632 (1867), holds that a tax on the excess of the market value of the stock over the value of the corporate realty and machinery, is a franchise tax. In Indiana it is held that a tax on the shares of stock is the proper mode of taxation, unless the statute provides otherwise. *Whitney v. City of Madison*, 23 Ind. 331 (1864). The mere fact that the corporation is compelled to pay the tax does not prevent its being considered a tax on the shares. *National Bank v. Commonwealth*, 9 Wall. 353, 360 (1869), per Miller J.

stock, even though the corporation is required to pay it and to collect the same from the owners of those shares.

§ 564. *Tax on stockholders residing in the State creating the corporation.*—The right of the State to tax resident stockholders of a resident corporation on their shares of stock is undoubted, and has been unquestioned, except where double taxation would result therefrom, or a constitutional provision restricts this mode of taxation.¹ Generally such a tax on resident stockholders is levied on them, not in the municipality where the corporation is, but in the cities, counties, or towns where the stockholders respectively reside. This is always the rule if the statute is silent, and is the rule unless the statute expressly provides otherwise.² Controversies sometimes arise as to the power of a municipality to tax stockholders living in the State, but not in the municipality, which levies a tax on the shares of stock which they own in a corporation located within that municipality.

The law plainly is that such a tax is unauthorized, illegal, and not collectible, unless the municipality is authorized by statute to levy the tax.³ A mere general authority to the municipality to tax all property within its boundaries, will authorize a tax by it

¹ In Illinois, under the act of 1872, taxing railroad corporations, resident stockholders in domestic corporations are not taxed. *Porter v. Rockford, &c., R. R. Co.*, 76 Ill. 561 (1875). In Iowa stock is taxed under § 813 of the Code. See *Cook v. City of Burlington*, 59 Iowa, 251 (1882). As to the valuation of the shares of stock, see *St. Charles, &c., R. R. Co. v. Assessors*, 31 La. Ann. 852 (1879). If the corporation owns shares of its own stock, it is taxable the same as though owned by another. *Richmond, &c., R. R. Co. v. Alamance Co.*, 84 N. C. 504.

² *City of Evansville v. Hall*, 14 Ind. 27 (1859). A pledger is the proper person to be assessed on stock which has been pledged. *Tucker v. Aiken*, 7 N. H. 113 (1834). A pledgee of stock is not subject to a tax levied on the shares of stock held by him. *Waltham Bank v. Waltham*, 51 Mass. 334 (1845). In Massachusetts, shares held by executors or administrators are taxed in the town of which the deceased was an inhabitant at the time of his death, and shares held by

trustees are taxed in the towns in which the *cestuis que trust* respectively reside. *Revere v. Boston*, 123 Mass. 375 (1877).

³ *Stetson v. City of Bangor*, 56 Me. 274 (1868), the court saying: "Municipalities can tax shares of stock only when authorized so to do by some law of the State. They are the creatures of State law, and derive their powers in this respect solely from State enactments." *Griffith v. Watson*, 19 Kan. 23 (1877); *City of Evansville v. Hall*, 14 Ind. 27 (1859); *Conwell v. Town of Connersville*, 15 Ind. 150 (1860). Such a tax may be levied under a general power of the municipality to tax property. *Gordon's Ex'rs v. Mayor, &c.*, 5 Gill (Md.), 231 (1847). *Cf. Richmond v. Daniels*, 14 Gratt. 385; *Augusta v. Nat. Bk.*, 37 Ga. 620. *Markoe v. Hartranft*, 6 Am. L. Reg. N. S. 487 (1867), holds that in Pennsylvania such a tax is unconstitutional, and that a tax must be levied where the stockholder resides. See also *Craft v. Tuttle*, 27 Ind. 332 (1866).

of shares of stock owned by persons living within it.¹ But such authority does not sustain a tax on stockholders residing out of the municipality, although within the State. The location of such shares of stock, as property for purposes of taxation, is not where the corporation is located, but where the stockholder lives.² The statutes of the State may change this *situs* of the stock, so as to render it taxable where the corporation is, but, unless there is a statute to that effect, such a tax by a municipality is unauthorized and void.

§ 565. *Tax on resident stockholders in a non-resident or foreign corporation.*—It is undoubtedly within the constitutional power of the legislature of a State to enact a statute that persons residing in that State, who are stockholders in a corporation created by another State, shall be taxed on his shares of stock, at their residence within the former State.³ This principle of law is based on the fact that shares of stock are personal property; that they are distinct from the corporate property, franchises, and capital stock; that they follow the domicile of their owner like other personal property, and that consequently he may be taxed therefor wherever he may reside. It accordingly is a question of policy and expediency with a State whether or not it will tax its citizens who are stockholders in foreign corporations. A few of the States, including Pennsylvania,⁴ levy such

¹ But a municipality can levy a tax only when specially authorized so to do, and can tax only such property as the statute permits it to tax. *Cooley on Taxation* (2d ed.) 678. Hence power to a municipality to levy a tax for watchmen purposes will not authorize a tax on shares of stock. *Bk. of Ga. v. Savannah, Dudley (Ga.)*, 130 (1832).

² See § 566.

³ *Worthington v. Sebastian*, 25 O. St. 1 (1874); *Bradley v. Bauder*, 36 O. St. 28 (1880), holding it valid although the corporation is taxed in the State where it exists. To same effect *Seward v. City of Rising Sun*, 79 Ind. 351 (1881); *Dyer v. Osborne*, 11 R. I. 321 (1876); *McKeen v. County of Northampton*, 49 Penn. St. 519 (1865); *Dwight v. Boston*, 12 Allen, 316 (1866); *Whitesell v. Id.*, Id. 526; *Great Barrington v. County Com'rs*, 83 Mass. 572 (1835); *Worth v. Com'rs*, 82 N. C. 420 (1880); s. c. 90 N. C. 409 (1884). In Illinois also, resident stock-

holders in foreign corporations are taxed on their shares of stock. *Porter v. Rockford, &c. R. R. Co.*, 76 Ill. 561 (1875); *Cooley on Taxation*, 2d ed. 57, 221; *Holton v. Bangor*, 23 Me. 264; *Smith v. Exeter*, 37 N. H. 556.

⁴ See Act of April 29, 1844. *Lycoming County v. Gamble*, 47 Penn. St. 106 (1864). See also *In re Short's Estate*, 16 Penn. St. 63 (1851), where a decedent, who died a resident of Pennsylvania, left a fortune in stocks of non-resident corporations. The stocks were held subject to a collateral inheritance tax. *State v. Hannibal & St. J. R. R. Co.*, 37 Mo. 265 (1866); *Sturges v. Carter*, 114 U. S. 511 (1884), upholding such a tax in Ohio; *Newark City Bk. v. Assessor*, 30 N. J. L. 1 (1862). See also *Webb v. Burlington*, 28 Vt. 188 (1856). California made a wise resolution when, in 1881, it repealed § 3640 of its Political Code, taxing shares of stock, and added the following, § 3608, to that Code: "Shares of stock in cor-

taxes. But New York pursues the more broad and liberal policy that corporate interests should be taxed where the corporation exists; that the State which creates, protects, and furnishes facilities to the corporation for the earning of dividends, should have the sole benefit of taxes on such corporate interests, that its tax on resident stockholders in non-resident corporations would generally result in a double taxation of stockholders not residing in the State creating the corporation, and that inter-State comity, interests, and financial investments are promoted best by each State taxing its own corporations directly, and no State levying a tax on either resident stockholders in non-resident corporations, or resident stockholders in resident corporations.¹ The injustice of a tax on resident stockholders in foreign corporations is at once apparent when it is considered that the State creating the corporation nearly always taxes the corporation itself or all its stockholders, resident and non-resident, and that if stockholders residing elsewhere are taxed again where they reside, they are

porations possess no intrinsic value over and above the actual value of the property of the corporation which they stand for and represent, and the assessment and taxation of such shares and also of the corporate property would be double taxation. Therefore all property belonging to corporations shall be assessed and taxed, but no assessment shall be made of shares of stock, nor shall any holder thereof be taxed therefor." Sustained and applied in *Burke v. Badlam*, 57 Cal. 602; *Spring Valley W. W. v. Schottler*, 62 Cal. 69, 118 (1882). But the temptation to tax stockholders in non-resident corporations was yielded to. See *San Francisco v. Fry*, 63 Cal. 470 (1883); *Id. v. Flood*, 64 Cal. 504 (1884). As to Ohio see R. S. 1886, §§ 2737, 2739, 2744, construed in *Jones v. Davis*, 35 O. St. 474 (1886). See also *Worth v. Com'rs of Ashe County*, 90 N. C. 409 (1884); *Seward v. City of Rising Sun*, 79 Ind. 351.

¹ 1 R. S. of N. Y. ch. XIII, title 1, § 7 (p. 982, 7th ed.), provides as follows: "The owner or holder of stock in any incorporated company liable to taxation on its capital, shall not be taxed as an individual for such stock." See also *People v. Com. of Taxes*, 4 Hun, 595 (1875), aff'g 62 N. Y. 630, holding that residents of this State, owning shares of stock in a corporation created under and by the

laws of this State, or of any foreign State, are not subject to be personally assessed and taxed thereon under the laws of this State. For the purpose, however, of making the taxation of moneyed corporations correspond to taxation of shareholders in national banks, and for the purpose of taxing the latter, the following statutes were passed: Laws of 1866, ch. 671; Laws of 1880, ch. 140; Laws of 1880, ch. 596; Laws of 1881, ch. 477; Laws of 1882, ch. 410, § 848. The tax generally levied on corporations in New York is held to be a tax on their franchises. See *People v. Home Ins. Co.*, 92 N. Y. 328 (1883); *Id. v. McLean*, 80 N. Y. 254 (1880); *Id. v. Ferguson*, 98 N. Y. 89 (1868); *Id. v. Williamsburgh Gas Light Co.*, 76 N. Y. 202. Laws of 1880, ch. 542, as am'd by Laws of 1881, ch. 361; also Laws of 1883, ch. 359. See *People v. New York, &c. Co.*, 92 N. Y. 487; *Id. v. Davenport*, 91 N. Y. 574; *Nassau, &c. Co. v. City of Brooklyn*, 89 N. Y. 409. So also in Missouri. See *Valle v. Ziegler*, 84 Mo. 214 (1884). See also *People v. Bradley*, 39 Iowa, 130 (1866). Cf. *Bk. of Republic v. County of Hamilton*, 21 Ill. 54 (1858). See also *Smith v. Exeter*, 37 N. H. 556 (1859), and *Jersey City Gas Light Co. v. Jersey City*, 46 N. J. L. 194 (1884).

taxed both in the State of the corporation, directly or indirectly, and also in the State where they reside directly. No reduction need be allowed in the latter State for taxation of the corporation levied in another State.¹

§ 566. *Tax on non-resident stockholders in resident or domestic corporation.*—When it is determined by a State that it prefers to levy a tax on shares of stock, rather than on the franchises, capital stock, or tangible property of the corporation, or to levy a tax on both, there is no doubt as to its right to tax the stockholders residing within the State. But more difficulty occurs as to the right of the State to tax non-resident stockholders in corporations created by the State. This right has been strenuously denied on the ground that shares of stock are not located at the domicile of the corporation, but follow the domicile of the stockholder.

It is the well-established rule, however, that although shares of stock have at common law no *situs* except the domicile of the shareholder, yet that a statute enacted by the State creating the corporation may give to the shares of stock a *situs* at the location of the corporation; that such a statute may thus determine the *situs* of shares of non-resident stockholders, without changing the *situs* of shares of resident stockholders; and that consequently, under a statute expressly authorizing such a tax, non-resident stockholders in a resident corporation may be taxed thereon, where the corporation has its domicile.² The method of enforce-

¹ See note 3, page 571.

² In the case of *Ottawa Glass Co. v. McCaleb*, 81 Ill. 556 (1876), the court said that the legislature might "require the taxes to be paid by the corporation, and collected by them of the shareholder, by deducting the amount from his dividends or otherwise." *State v. Mayhew*, 2 Gill (Md.), 487 (1845), where the corporation was to pay the tax from dividends if declared, and from profits if no dividends were declared. *St. Albans v. National Car Co.*, 57 Vt. 68 (1884), holding that the statute giving shares of stock a *situs* at the location of the corporation may be passed after the incorporation, and that *mandamus* lies to compel the corporation to pay the tax. In the case *Tappan v. Merchants Nat'l Bk.*, 19 Wall. 490, 499 (1873), the court said: "Personal property, in the absence of any law to the

contrary, follows the person of the owner, and has its *situs* at his domicile. But, for the purpose of taxation, it may be separated from him, and he may be taxed on its account at the place where it is actually located. See also *Whitney v. Ragsdale*, 33 Ind. 107 (1870); *Tallman v. Butler Co.*, 12 Iowa, 531; *Faxon v. McCarter*, Id. 527; *Mayor, &c. of Baltimore v. Baltimore, &c. Ry. Co.*, 57 Md. 31 (1881). The last case holds that stock in street railways in Maryland may be taxed, although, by statute, stock in steam railways cannot be. See, however, *City of Richmand v. Daniel*, 14 Gratt. (Va.) 385 (1858); also the case *Oliver v. Washington Mills*, 93 Mass. 268 (1866), which holds such a tax to be unconstitutional. The common law rule is well expressed in *Union Bk. v. State*, 9 Yerg. (Tenn.) 490 (1836), where the court says: "The

ing the payment of this tax may be by compelling the corporation to pay it and giving it a lien therefor on the stock, or authorizing it to deduct the tax from the non-resident stockholders' dividends; or, if the statute is silent as to the mode of collection, an attachment and execution therefor, may be levied on the shares of stock.¹ In New York, where neither resident

power to tax non-resident stockholders is denied, and we think correctly; from its very nature it must be a tax in *personam* and not in *rem*. Stock is in the nature of a chose in action and can have no locality; it must, therefore, of necessity follow the person of the owner. . . . Bankstock is not a thing in itself capable of being taxed on account of its locality, and any tax imposed upon it must be in the nature of a tax upon income and of necessity confined to the person of the owner, and if he be a non-resident he is beyond the jurisdiction of the State and not subject to her laws." See also *Minot v. Railroad Co.*, 18 Wall. 276; *City of Davenport v. Miss. & Mo. R. R. Co.*, 12 Iowa, 539 (1861); *Howell v. Cassopolis*, 35 Mich. 471 (1877). In *Bradley v. Bauder*, 36 O. St. 28 (1880), the court said, "that shares of stock may be separated from the person of the owner, by statute, and given a *situs* of their own, was held in *Tappan v. Merchant's Nat. Bk.*, 19 Wall. 490. But when not so separated, that this *situs* follows and adheres to the domicile of the owner, is supported by a great weight of authority." See *State Tax on Foreign-held Bonds*, 15 Wall. 300 (1872). See also *Jenkins v. Charleston*, 5 S. C. 393 (1874). In *Nat'l Com. Bk. v. Mobile*, 62 Ala. 284 (1878), the court well says: "It may be made the duty of a bank to pay for its shareholders the tax legally assessed against their respective shares, whether the stockholders reside in the State of Alabama or not, Contestations upon these points have been made time and again, sometimes by the banks and sometimes by the shareholders, to avoid this liability. But it is established by repeated adjudications, and ought to be considered definitely settled." And in *First Nat'l Bk. v. Smith*, 65 Ill. 44 (1872), the court says: "The separation of the *situs* of personal property from the domicile of the owner, for the purposes of taxation, is familiar doctrine in the courts of this country, and has been sanctioned by this court in various cases. . . . The act of Congress itself contemplates a severance of the *situs* of such shares from the

person of their owner, by providing that they should not be taxed except in the State where the bank is established. But, apart from this, it is really much more reasonable to fix the *situs* of shares at the place where the bank is located, and where it must continue to do its business or wind up its affairs, than to separate by legislation tangible personal property from the person of its owner." In the case *St. Louis Nat'l Bk. v. Papin*, 4 Dill. 29 (1876), the following statute was sustained: "The taxes assessed on shares of stock embraced in such list shall be paid by the corporations respectively, and they may recover from the owners of such shares the amount so paid by them, or deduct the same from the dividends accruing on such shares, and the amount so paid shall be a lien on such shares respectively, and shall be paid before a transfer thereof can be made." And again in *American Coal Co. v. County Com'rs*, 59 Md. 185 (1882), the court says: "The State may give the shares of stock held by individual stockholders a special or particular *situs* for purposes of taxation, and may provide special modes for the collection of the tax levied thereon."

¹ In *Farrington v. Tennessee*, 95 U. S. 679, 687 (1877), the court says: "The bank may be required to pay the tax out of its corporate funds, or be authorized to deduct the amount paid for each stockholder out of his dividend." And, in general, under the act of Congress allowing taxation of shares of stock in national banks, a *situs* is given by statute to the shares so as to locate them where the bank is located, even though the shareholders be non-resident. But collections cannot be enforced against the corporation unless the statute specially authorizes it. *First Nat'l Bk. v. Fancher*, 48 N. Y. 524 (1872). Collection by execution, see *Gordon's Ex'rs v. Mayor, &c.* 5 Gill (Md.), 231 (1847). But a levy of execution on stock can only exist when the statute allows stock to be so taken. *Barnes v. Hall*, 55 Vt. 420 (1883); or under a tax warrant, *McNeal v. Mechanics, &c.*

nor non-resident stockholders, in either foreign or domestic corporations, excepting banking corporations, are taxed on their shares of stock, these inter-State complications, hardships, and jealousies do not arise.¹

§ 567. *Double taxation.*—The most objectionable feature of a tax levied on shares of stock, is that almost inevitably it operates to impair a double tax on a part or all of the stockholders.² Such a double tax exists where either the corporate realty or personalty, or franchise or capital is taxed, and a tax is also levied on the shares of stock without any deduction for the former taxation.³ There has been some controversy as to the right of a State to levy a double tax on property. Sometimes the State constitution prohibits such taxation.⁴ But aside from constitu-

Ass'n, 12 Am. & Eng. Corp. Cas. 181 (N. J. 1885). See also Chapter on Attachment and Execution. In the case of *State v. Thomas*, 26 N. J. L. 181 (1857), the court refused to compel the corporation to pay the tax on stock of non-residents and said: "It has been decided by this court that the bonds and stocks of corporations in this State held by non-residents are not liable to taxation, though they are clearly within the letter of the act." A State may collect a non-resident stockholder's tax from the corporation and give it a lien therefor on his stock. *North Ward Nat'l Bk. v. City of Newark*, 39 N. J. L. 380 (1877); but see *Raleigh, &c. R. R. Co. v. Conner*, 87 N. C. 414. *Cooley on Taxation*, 2d ed. 433, clearly upholds the rule that the State may levy a tax on shares of stock and compel the corporation to pay it, citing *Maltby v. Reading R. R. Co.*, 52 Penn. St. 140; *Haight v. Railroad Co.*, 6 Wall. 15; *National Bank v. Commonwealth*, 9 Wall. 353; *United States v. Railroad Co.*, 17 Wall. 322; *Minot v. Railroad Co.*, 18 Wall. 206; *Ottawa, &c. v. McCaleb*, 81 Ill. 556; *New Orleans v. Saving, &c. Co.*, 31 La. Ann. 826; *Baltimore v. City Passenger R. Co.* 57 Md. 31; *St. Albans v. National Car Co.*, 57 Vt. 68; *American Coal Co. v. Allegany County*, 59 Md. 185; *Barney v. State*, 42 Md. 480; *McVeagh v. Chicago*, 49 Ill. 318; *First Nat'l Bk. v. Fancher*, 48 N. Y. 524; *Leonberger v. Rowse*, 43 Mo. 67; *Relfe v. Life Ins. Co.*, 11 Mo. App. 374.

¹ See § 565, note.

² In Ohio such double taxation is boldly advocated and recommended. In *Frazer v. Seibern*, 16 O. St. 614 (1866), the court said, in advocating an equitable system of taxation: "That object is best attained in case of a corporation, or joint-stock company, by taxing the stockholders, the persons who own its property, upon the full value of their shares therein, including, of course, their interest in the franchise or privilege, and in all tangible property owned by the company; and by taxing the corporation also upon the value of such tangible property. The stockholders are thus taxed, as all other individuals who own tangible and intangible property are sometimes unavoidably taxed, once upon all he is worth, and a second time upon that part of his property which is tangible."

³ This is practically the result. In the case *Farrington v. Tennessee*, 95 U. S. 679, 687 (1877), however, the court says in a *dictum*: "The capital stock and the shares may both be taxed, and it is not double taxation." *Cf. Ryan v. Comrs.*, 30 Kan. 185 (1883).

⁴ *County Comrs. v. Farmers Natl. Bk.*, 48 Md. 117 (1877), the constitution saying that each person shall pay a tax "according to his actual worth in real or personal property." See also *City of San Francisco v. Mackey*, 21 Fed. Rep. 539 (1884); *Burke v. Badlam*, 57 Cal. 594 (1881), relative to the California Constitution, Art. XII, § 1, that "all property shall be taxed in proportion to its value."

tional restrictions, it unquestionably is within the power of the State, to levy not only a double tax, but even a treble or quadruple tax, if it so chooses.¹ The injustice of such taxation, however, generally prevents its occurrence. The courts also do their utmost to prevent double taxation, and will construe a taxation statute so as to avoid such a result, and sometimes even in opposition to the plain words of the statute itself.²

§ 568. *Exemptions from taxation as affecting tax on shares of stock.*—An exemption of shares of stock, is a contract protected by that provision of the Constitution of the United States, which prevents a State from passing a law which will impair the validity of contracts.³ Aside from questions of this nature, there are two classes of cases of exemptions from taxation which affect the taxation of shares of stock. The first class involves the question whether an exemption of the corporate property, franchises, or capital stock from taxation, exempts also the shares of stock

¹ *Salem Iron, &c., Co. v. Danvers*, 10 Mass. 514 (1813), where corporate realty was taxed, although the shares of stock were also taxed. See also *Belo v. Comrs. of Forsyth*, 82 N. C. 415 (1880). In the remarkable case of *Tall Bridge Co. v. Osborn*, 35 Conn. 7 (1868), it seems that the realty, capital stock, and shares of stock of a corporation were taxed, and that the chief stockholder, a railroad, was taxed on its capital stock and shares of stock, making four or five taxations of the same property. Evidently corporations were not popular in Connecticut in 1868, except for taxation purposes. Cf. *Jones, &c., Co. v. Commonwealth*, 69 Penn. St. 137. See also *Cook v. City of Burlington*, 59 Iowa, 251 (1882); *State v. Branin*, 23 N. J. L. 484 (1852); *Id. v. Bentley*, *Id.* 532; *City of Memphis v. Ensley*, 6 Bax. (Tenn.) 553 (1873); *Prov., &c., R. Co. v. Wright*, 2 R. I. 459, 464 (1853), holding that a tax on the stock does not raise a presumption that a municipality is thereby prevented from taxing the corporate realty. See also *Hannibal, &c., R. R. Co. v. Shacklett*, 30 Mo. 550, 560 (1860).

² Thus in Illinois, in cases where the capital stock is taxed by the State, the shares of stock are held to be free from taxation. *Republic Life Ins. Co. v. Pollok*, 75 Ill. 292 (1874). See also *County of Lackawanna v. First Natl. Bk.*, 94 Penn. St. 221 (1880), holding that under the Act of March 31, 1870, releasing cor-

porations from all other taxes, if they pay a one per cent. tax on the par value of the stock, the corporate realty cannot be taxed, after such one per cent. has been paid. *State v. Hannibal & St. J. R. R. Co.*, 37 Mo. 265 (1866); *Jersey City, &c., Co. v. Jersey City*, 46 N. J. L. 194 (1884); *Cheshire, &c., Telephone Co. v. State*, 63 N. H. 167 (1884); *Valle v. Zeigler*, 84 Mo. 214 (1884); *Tax Cases*, 12 G. & J. (Md.) 117 (1841); *Prov. Inst. for Sav. v. Gardiner*, 4 R. I. 484 (1857); *Mechanics Bk. v. Thomas*, 26 N. J. L. 181 (1857); *American Bk. v. Mumford*, *Id.* 478 (1857); *State v. Tunis*, 23 N. J. L. 546 (1852); *Smith v. Burley*, 9 N. H. 423 (1838); *Frazer v. Siebern*, 16 O. St. 614; *Savings Bk. v. Nashua*, 46 N. H. 389 (1866), the court saying: "It is a fundamental principle in taxation, that the same property shall not be subject to a double tax, payable by the same party, either directly or indirectly, and where it is once decided that any kind or class of property is liable to be taxed under one provision of the statutes, it has been held to follow as a legal conclusion, that the legislature could not have intended the same property would be subject to another tax, though there may be general errors in the law, which would seem to imply that it was to be taxed a second time."

³ *Farrington v. Tennessee*, 95 U. S. 679 (1877).

from any tax; the second, whether an exemption of the shares of stock from taxation, exempts the corporate property, franchises, and capital stock. As regards the former exemption, the effect thereof depends largely on the words used in the statute or charter granting the exemption. The question has given rise to a difference of opinions. In the Federal courts, New Jersey, Indiana, and Kentucky, it has been decided that an exemption of the corporation from taxation on one or more of the first three methods of taxation exempts by implication the shares of stock.¹ But in Tennessee, North Carolina, and Maryland, a contrary rule prevails.²

As regards the second class of exemptions, it seems to be established by the great weight of authority that an exemption of the shares of stock from taxation exempts also, by implication, the corporate franchises, capital stock, and tangible property from

¹ *State v. Branin*, 23 N. J. L. 484 (1852); *Id. v. Bentley*, *Id.* 532; *Johnson v. Commonwealth*, 7 Dana (Ky.), 338 (1838); *King v. City of Madison*, 17 Ind. 48 (1861), holding that an exemption of the capital stock exempts shares of stock. *Gordon v. Appeal Tax Court*, 3 How. 133 (1845), held that an exemption prohibiting any "further tax or burden upon them" the banks, exempted the shares of stock. Again, where the charter provided that "the capital stock of said company shall be forever exempt from taxation, the shares of stock cannot be taxed. . . . Each share is a part of the whole, and, as the whole is exempt from taxation, it follows that each part or share must also be exempt." *State of Tenn. v. Whitworth*, 22 Fed. Rep. 75 (1884). And the purchaser and successor of a railroad, taking by statute all its rights and privileges, is also exempt in same manner. *Id.*, 81; *aff'd*, 117 U. S. 139 (1886). An exemption of shares of stock from taxation is waived by the acceptance of subsequent statutes imposing a tax. *Hannibal & St. J. R. R. Co. v. Shacklett*, 30 Mo. 550 (1860); *Cooley on Taxation*, 2d ed. 212.

² *Union Bk. v. State*, 9 Yerg. (Tenn.) 490 (1836), holding that an exemption of the capital stock did not exempt shares of stock. To same effect, *City of Memphis v. Farrington*, 8 Baxter (Tenn.), 539 (1876), the court saying: "The capital stock and shares of stock are two distinct properties, and an exemption of the one does not thereby necessarily exempt the other, nor the taxation of the latter, oper-

ate as a tax on the former, so as to interfere with its exemption from such burdens." *Belo v. Comrs. of Forsyth*, 82 N. C. 415 (1880), holding that an exemption of the corporate realty does not exempt the shares of stock. *Appeal Tax Court v. Rice*, 50 Md. 302 (1878); *Tax Cases*, 12 G. & J. (Md.) 117 (1841). In the case *County Comrs. v. Annapolis, &c. R. R. Co.*, 47 Md. 592 (1877), the court says: "To make out the claim to this exemption from the taxing power of the State, so essential to the support of its government, it is incumbent upon corporation to show that the power to tax has been clearly relinquished by the State; and if this has not been done in clear and explicit terms, or by necessary implication, the question whether or not the exemption has been granted, must be resolved in favor of the State." *Citing Prov. Bk. v. Billings*, 4 Pet. 514; *Wilmington R. R. Co. v. Reid*, 13 Wall. 264; *Phil. & Wilmington R. R. Co. v. State*, 10 How. 376. But a clear exemption of the shares of stock is a contract which is protected by the United States Constitution. *State v. Baltimore & O. R. R. Co.*, 48 Md. 49 (1877). A charter provision, however, that a certain tax shall be paid by the corporation, does not prevent a subsequent change in that tax. *Delaware Railroad Tax*, 18 Wall. 206 (1873). And an exemption by the State has been held not to exempt from taxation of the shares by a municipality. *Gordon's Exrs. v. Mayor, &c.*, 5 Gill (Md.), 231 (1847).

any tax.¹ Exemptions, however, have no effect, and are of no avail beyond the boundaries of the State granting them; and, accordingly, a non-resident stockholder, who is taxed on his stock in the State where he resides, cannot defeat that tax by reason of exemptions enjoyed within the State creating the corporation.²

§ 569. *Taxation of national bank stock.*—It is one of the established principles of constitutional law in this country that the instruments of government by the United States shall not be taxed by any State, and also that those of a State shall not be taxed by the United States. Accordingly, the bonds issued by the United States government cannot be taxed by any State.³ So also, when the old United States Bank was in existence, it was held that neither the bank nor its capital stock could be taxed by a State. But it was also held that, inasmuch as the interest of the stockholders in the bank was different from the franchises, property, capital stock, and United States bonds held by the bank, such interest of the shareholder could be taxed by a State, and that such taxation would be constitutional and legal.⁴ The same rules apply to the present national banks. A State tax on the capital stock of the bank is illegal and void.⁵ But a tax on

¹ *Scotland Co. v. Mo., Iowa, &c., Ry. Co.*, 65 Mo. 123 (1877), the court saying: "It is clear that a tax on the property represented by the stock is substantially a tax on the stock." See also *County Comrs. v. Annapolis, &c., R. R. Co.*, 47 Md. 592 (1877), where the court says: "It is settled by repeated decisions of this court, which we are not disposed to disturb, that the exemption of the shares of the capital stock operates as an exemption of the property of the corporation, or so much of it as the corporation is fairly authorized to hold for the proper exercise of its franchises; and this upon the principle that the shares of the stock in the hands of the shareholders represent the property held by the corporation." *Bk. of Cape Fear v. Edwards*, 5 Ired. Law (N. C.), 516 (1845), where the charter said: "the said bank shall not be liable to any further tax." *Mayor, &c., of Baltimore v. Baltimore & O. R. R. Co.*, 6 Gill (Md.), 288 (1848); *Tax Cases*, 12 G. & J. (Md.) 117 (1841); *Gordon's Exrs. v. Mayor, &c., of Baltimore*, 5 Gill (Md.), 231 (1847). In the case, however, of *Wilmington & W. R. R. Co. v. Reid*, 64 N. C. 226 (1870), it was held that an ex-

emption of shares of stock does not exempt the corporate franchise from taxation. And in *State v. Petway*, 2 Jones' Eq. (N. C.) 396 (1856), it was held that a charter provision that the shares of stock should be taxed a certain amount, did not prevent a tax on dividends.

² *Appeal Tax Court v. Patterson*, 50 Md. 354 (1878); *Id. v. Gill*, *Id.* 377. See also *Railroad Co. v. Pennsylvania*, 15 Wall. 300 (1872).

³ *Cooley on Taxation*, 2d ed., 84, 85. Formerly government bonds were called stock, both in England and in this country. This use of the term, however, has become practically obsolete. See *Bk. of Commerce v. New York*, 2 Black. 620 (1862); *Weston v. City, &c., of Charleston*, 2 Peters, 449 (1829).

⁴ *National Bk. v. Commonwealth*, 9 Wall. 353 (1869), per Miller, J.; *McCulloch v. State of Maryland*, 4 Wheat. 316, 436 (1819); *Bulow v. City of Charleston*, 1 Nott & McCord (S. C.), 527 (1819). See also *Berney v. Tax Collector*, 2 Bailey (S. C.), 654 (1831).

⁵ *Bk. of Omaha v. Douglas County*, 3 Dill. 298 (1873); *Salt Lake, &c., Bk. v. Golding*, 2 Utah, 1 (1876); *Mayor, &c.,*

its real estate or on its shares of stock is upheld as legal and enforceable.¹ This is the law, although a large part or all of the bank's capital stock is invested in United States bonds.² The authority of a State to tax shares of stock in national banks is expressly conferred by the statutes of the United States, which create and regulate these banks.³ The only questions of impor-

of *Macon v. First Natl. Bk.*, 59 Ga. 648 (1877); *Bradley v. Illinois*, 6 Am. L. Reg. N. S. 486; *Bk. of Commerce v. N. Y. City*, 2 Black. 620; reversing *People v. Comrs. of Assessments*, 23 N. Y. 192; s. c., 32 Barb. 509, and declaring unconstitutional the New York statutes, under which the national banks were taxed. New York has been exceedingly unfortunate in its efforts to tax national banks. After the decision in *Bk. of Commerce v. N. Y. City*, *supra*, came *Bank Tax Case*, 2 Wall. 200 (1864), declaring unconstitutional the New York statute of 29th April, 1863, for the taxation of national banks, the tax still being on the capital stock. Next came *Van Allen v. The Assessors*, 3 Wall. 573 (1865) (reversing *City of Utica v. Churchill*, 33 N. Y. 161. See also *First National Bk. v. Fancher*, 48 N. Y. 524, 1872), declaring unconstitutional the New York statute of 9th March, 1865, taxing the shareholders in national banks, because the act did not prescribe expressly that the tax should be no greater than the tax on other shares of stock, and because taxes in New York on other corporations were not on shares of stock but on the capital stock. New York then passed the Act of 23d April, 1866, which was sustained in *People v. Comrs.*, 4 Wall. 244 (1866). Still later came the case of *People v. Weaver*, 100 U. S. 539 (1879), declaring void the New York tax of national bank stock, for the reason that the New York Court of Appeals construed the New York taxation statute to allow persons taxed on ordinary securities a deduction for debts, while a similar deduction was not allowed to stockholders in banks, State or National. *Supervisors v. Stanley*, 105 U. S. 305 (1881) [see *People v. Dolan*, 36 N. Y. 59, 1867], practically modified the preceding case, however, by holding that a stockholder who owed no debts could not complain, and that those who did owe debts were entitled, not to a release from the tax altogether, but only to the extent of what the State ought to have allowed as a deduction. The last case in New York was

decided by Judge Wallace, in November, 1886, sustaining the State tax of shares of stock in national banks. It has been held that a State may tax bank notes, but not treasury notes—i. e., "greenbacks." *Bd. of Comrs. v. Elston*, 32 Ind. 27 (1869).

¹ *Austin v. Boston*, 96 Mass. 359 (1867); *First Natl. Bk. v. Douglas County*, 5 Dill. 330 (1874), upholding the Nebraska statute herein of 27th February, 1873. *Stetson v. City of Bangor*, 56 Me. 274 (1868).

² *Van Allen v. Assessors*, 3 Wall. 573 (1865); *People v. Comrs.*, 4 Wall. 244 (1866).

³ Rev. Stat. U. S. § 5219 (taken from act of 3d June, 1864, as amended by act of February 10th, 1868): "Nothing herein shall prevent all the shares in any association from being included in the valuation of the personal property of the owner or holder of such shares, in assessing taxes imposed by authority of the State within which the association is located; but the legislature of each State may determine and direct the manner and place of taxing all the shares of national banking associations located within the State, subject only to the two restrictions, that the taxation shall not be at a greater rate than is assessed upon other moneyed capital in the hands of individual citizens of such State, and that the shares of any national banking association, owned by non residents of any State, shall be taxed in the city or town where the bank is located, and not elsewhere. Nothing herein shall be construed to exempt the real property of associations from either State, county, or municipal taxes, to the same extent, according to its value, as other real property is taxed." The case of *People v. Weaver*, 100 U. S. 539, 543 (1879), says that the effect of the Act of Congress, as regards the taxation of national banks, is that Congress says to the States: "You may tax the real estate of the banks as other real estate is taxed, and you may tax the shares of the bank as the personal property of the owner to the same extent you tax other moneyed

tance that are still unsettled, turn upon the meaning and application of that statute, and, accordingly, the law is stated most clearly when it is connected with the various provisions of these statutes.

§ 570. *Place in which shares of national bank stock may be taxed.*—The Revised Statutes of the United States expressly declare that non-resident stockholders in a national bank are to be taxed at the place where the bank is located.¹ Under this statute, a non-resident of the State within which the bank is situated can be taxed on his stock only where the bank is located.² The State where he resides cannot also tax him on such stock. As regards residents of the State within which the bank is located, the State itself determines where the tax is to be levied.³ If the State statute requires that the whole tax shall be paid in the city, county, or town where the bank is located, even though some of the stockholders reside in other counties or cities, the statute must be obeyed.⁴ Generally, however, the statute requires that stockholders residing in the State shall be taxed at their place of residence on stock owned by them in a national bank within that State.⁵ If the statute is silent herein, then the State statutes

capital invested in your State. It was conceived that by this qualification of the power of taxation equality would be secured and injustice prevented." In *Watson v. First Natl. Bk.*, 8 Northeast. Rep. 97 (Ind., 1886), the court says: "It has been many times held by the Supreme Court of the United States that the authority of the States to tax the shares of national bank stock is derived wholly from the . . . Act of Congress, and that without the consent of Congress these bank stock shares could not be taxed by State authorities at all."

¹ Such was the effect of the amendment of 1866. Previous to that time there was controversy herein as to the meaning of the act of 1863. See *Austin v. Boston*, 96 Mass. 359 (1867).

² See *McIver v. Robinson*, 58 Ala. 456; *Weaver v. Weaver*, 75 N. Y. 30; *Kyle v. Fayetteville*, 75 N. C. 445; *Natl. Bk. v. Commonwealth*, 9 Wall. 353; *Lionberger v. Rowse*, 9 Wall. 468.

³ *Austin v. Aldermen*, 7 Wall. 694 (1866). The tax may be levied on resident stockholders in the city, county, or town where they reside. *Austin v. Boston*, 96 Mass. 359 (1867). And the cash-

ier of the bank may be required by statute to send to the clerks of the various towns the names of such stockholders as reside in those towns. *Waite v. Dowley*, 94 U. S. 527 (1876).

⁴ *National Bank v. Commonwealth*, 9 Wall. 353 (1869); *Tappan v. Merchants' Nat. Bk.*, 19 Wall. 490 (1873); *Prov. Inst. v. City of Boston*, 101 Mass. 575 (1869); *McLaughlin v. Chadwell*, 7 Heisk. (Tenn.) 389 (1872); *Craft v. Tuttle*, 27 Ind. 332 (1866), holds that if a municipality has no power to tax shares in State banks, it cannot tax national bank shares.

⁵ *Clapp v. City of Burlington*, 42 Vt. 579 (1870). See *Trustees of Eminence v. Deposit Bk.* 12 Bush, 538; *Farmers' Nat. Bk. v. Cook*, 32 N. J. L. 347 (1867). *Off. State v. Hart*, 31 N. J. L. 434 (1866); *State v. Haight*, 31 N. J. L. 399 (1866), objectionable and unfortunate decisions in all respects. The decision in *Tenth Ward Nat. Bk. v. City of Newark*, 39 N. J. L. 380 (1877), however, placed New Jersey among the States which levy the tax in the most approved manner, residents being taxed where they reside, non-residents being taxed at the domicile of the corporation. See also *Kyle v.*

regulating the taxation of stockholders in other corporations are to apply to stockholders in national banks situated within the State.

§ 571. *The tax must not be greater than that imposed on other "moneyed capital."*—The most difficult, unsettled, and litigated questions connected with the taxation of shares of stock, in national banks, arise from the meaning and application of that provision of the statutes of the United States requiring that the taxation of national bank shares of stock shall not be at a higher rate than the taxation of other "moneyed capital" within the State. The words "moneyed capital" has been construed to mean, "not only bonds, stocks, and money loaned, but all credits and demands of every character in favor of the tax-payer."¹ Accordingly, it is not enough that the tax levied on shares in national banks is the same as that levied on shares in other banks or other corporations. It must be no greater than that levied on other forms of moneyed capital.² A different view, however, has been taken in a few cases.³ The method of taxing shares of stock, it has been held, should correspond to that followed in tax-

Mayor, &c., 75 N. C. 445 (1876); Buell v. Com'rs of Fayetteville, 79 N. C. 267 (1878); Austin v. City of Boston, 96 Mass. 359 (1867); First Nat. Bk. v. Smith, 65 Ill. 44 (1872); Baker v. First Nat. Bk. 67 Ill. 297 (1873); Clapp v. City of Burlington, 42 Vt. 579 (1870); Howell v. Cassopolis, 35 Mich. 471 (1877). Cf. Mintzer v. County of Montgomery, 54 Penn. St. 139 (1867).

¹ Wasson v. First Nat. Bk., 8 North-east. Rep. 87 (Ind. 1886); Boyer v. Boyer, 113 U. S. 689; see also Hepburn v. School Directors, 23 Wall. 480 (1874).

² In the case *People v. Commissioners*, 4 Wall. 256, this statutory provision is held to mean "that the rate of taxation upon the shares should be the same or not greater than upon the moneyed capital of the individual citizen which is liable to taxation; that is, no greater in proportion or percentage of tax in the valuation of shares should be levied than upon other moneyed taxable capital in the hands of the citizen." In *Adams v. Nashville*, 95 U. S. 19 (1877), the court said that the statute "simply required that capital invested in national banks should not be taxed at a greater rate than like property similarly invested."

³ A recent case in New York, *In re McMahon*, 102 N. Y. 176 (1886), holds that shares of stock in railroad, manufacturing, and other corporations, are not "moneyed capital" in the sense in which these terms are used in the Act of Congress. See also *First Nat. Bk. v. Waters*, 19 Blatch. 242; *Prov. Inst. v. City of Boston*, 101 Mass. 575 (1869), holds that the comparison is to be made with other moneyed capital in the same town or city where the tax is levied. So also *People v. Moore*, Idaho, 504 (1873). Subject to this rule the shares of national banks may be assessed at their value, even above par. *Hepburn v. School Directors*, *supra*; *People v. Commissioners*, &c., 94 U. S. 415 (1876); *Id.* 67 N. Y. 516 (1876); *aff'd* 8 Hun, 536. *St. Louis National Bk. v. Papin*, 4 Dill. 29 (1876), the court saying also that the assessors may ascertain that value by including "all reserve funds, profits, earnings, and other values" when the intent of the statute is to base the tax "upon an inquiry, *inter alia*, into the actual value of the property of the banks, so far as this imparts or confers a value upon the shares."

ing other corporations in the State.¹ Thus, it has been held that a tax cannot be levied on national bank stock, where there is no tax on stock in other corporations, the tax being upon the capital stock or franchises of the latter.² The material point, however, is that national bank stock must not, as a result, be taxed higher than other moneyed investments. If this rule is observed, it is of little consequence whether the tax on national bank stock is levied and assessed in the same way as other corporations are taxed.

If the State laws allow a deduction to a person taxed on bonds, notes, and similar property, for debts due from him to others, a similar deduction must be allowed to stockholders taxed on their shares in a national bank.³ If the statute does not allow the same to the latter, and the courts of the State refuses to allow the deduction, then the tax is illegal. Such was the result of a tax in New York on national bank stock.⁴ A refusal to allow a deduc-

¹ The mode of collection need not be the same. The State may compel the bank to pay the tax. *National Bk. v. Commonwealth*, 9 Wall. 353, 363 (1869), per Miller, J. But if the assessment is illegal in that no notice and opportunity is given to the shareholder to appear and resist the tax, it cannot be enforced. *Albany City Nat. Bk. v. Maher*, 20 Blatch. 341 (1882).

² *Van Allen v. Assessors*, 3 Wall. 573; *Bradley v. People*, 4 Wall. 459 (1866); *Hubbard v. Johnson County*, 23 Iowa, 130 (1867); *People v. Assessors*, 29 How. Pr. 371 (1865); *Wright v. Stelz*, 27 Ind. 338 (1866), overruling *Whitney v. Madison*, 23 Ind. 231, on certain points. *Cooley on Taxation*, 2d ed. 390. *Contra*, *People v. Bradley*, 39 Ill. 130 (1866). See also *Frazier v. Siebern*, 16 O. St. 614, *Smith v. First Nat. Bk.*, 17 Mich. 479. Where a State and also a local tax is levied on shares of stock in a State bank, and the local tax is declared illegal, the same local tax is illegal as regards shares in national banks, if such local tax is larger than the State tax. *City Nat. Bk. v. Paducah*, 2 Flippin, 61 (1877).

³ *Evansville Bk. v. Britton*, 105 U. S. 322 (1881), aff'g 8 Fed. Rep. 867. But a deduction to individuals for United States bonds held by them will not invalidate a tax on the national bank stock without a similar deduction. *People v. Comrs.*, 4 Wall. 244 (1866). In the recent case *Wasson v. First Natl. Bk.*, 8 Northeast. Rep. 97 (1886), the court held that deduction

allowed to others is fatal to a tax on national bank shares without that deduction only when it is "material and serious," and that that depends on the proportion of moneyed capital which is allowed the deduction to that moneyed capital which is not allowed it. If material, the national bank share tax is to be allowed a similar deduction. Where a tax on stock is not illegal, except in that the assessors have proceeded in a wrong manner, the court will not enjoin its collection, unless the plaintiff stockholders pay in such a tax as would have been legal. *Frazier v. Seibern*, 16 O. St. 614 (1866); *Cummings v. Merchants Natl. Bk.*, 401 U. S. 153 (1879); *Supervisors v. Stanley*, 105 U. S. 305 (1881); reversing *Hills v. Exchange Bk.*, 105 U. S. 319 (1881); rev'g. *Natl. Albany Exchange Bank v. Wells*, 18 Blatch. 478 (1880); 5 Fed. Rep. 348. Cf. *City Natl. Bk. v. Paducah*, 2 Flippin, 61 (1877). And a deduction to other moneyed corporations for their real estate must be allowed in taxing national bank shares. *Pollard v. State*, 65 Ala. 528 (1880); overruling *Melver v. Robinson*, 53 Ala. 456, and *Sumbre County v. Natl. Bk.*, 62 Ala. 464. In general, see also *Ruggles v. City of Fond de Lac*, 53 Wis. 436 (1881); *Miller v. Heilbron*, 58 Cal. 133 (1881); *St. Louis Natl. Bk. v. Papin*, 4 Dill. 29; *Covington, &c., Bk. v. Covington*, 21 Fed. Rep. 484; *Exchange Natl. Bk. v. Miller*, 19 Id. 372.

⁴ *People v. Weaver*, 100 U. S. 539 (1879). The New York court held that "the effect of the State law is to permit a

tion to stockholders in national banks similar to a deduction allowed on a tax levied on other "moneyed capital" was held to be a discrimination in contravention of the statute. Special exemptions, however, of certain stocks or other forms of "moneyed capital" do not require that a similar exemption should be made on national bank stock.¹

Again, the National Bank Act cannot be evaded by an unfair assessment of the shares in national banks, as compared with the assessment of other moneyed capital. It is a well known fact and an understood matter in nearly all localities, that no kinds of property are valued at their actual selling worth, in making the valuation for taxation purposes. Consequently if other moneyed capital is valued, in the assessment rolls, at a certain proportion of the actual value, and national bank stock at a higher proportion, the tax is illegal and cannot be collected.²

citizen of New York, who has moneyed capital invested, otherwise than in banks, to deduct from that capital the sum of all his debts, leaving the remainder alone subject to taxation, while he whose money is invested in shares of bank stock can make no such deduction." The Supreme Court of the United States declare the tax on the national bank shares to be invalid. But the case of *Supervisors v. Stanley*, 105 U. S. 305, 315 (1881), holds that the tax is not void absolutely. If the stockholder owed no debts he is not injured. And even if he owes debts, he cannot defeat the tax altogether, but is allowed a similar deduction.

¹ Thus a special contract exemption of a few State bonds from taxation, will not exempt the national bonds. *Lionberger v. Rowse*, 9 Wall. 468 (1869); *Hepburn v. School Directors*, 23 Wall. 480 (1874), where an exemption of mortgages, judgments, and contracts to sell land were immaterial herein. See also *Adams v. Nashville*, 95 U. S. 19 (1877); *Supervisors v. Stanley*, 105 U. S. 305, 317 (1881); *In re McMahon*, 102 N. Y. 176 (1886); *McLoughlin v. Chadwell*, 7 Heisk. (Tenn.) 389 (1872); *Boyer v. Boyer*, 113 U. S. 689; *Everitt's Appeal*, 77 Penn. St. 216; *Albany, &c., Bk. v. Maher*, 19 Blatch. 175.

² *Pelton v. National Bk.*, 101 U. S. 143 (1879), the court saying that "any system of assessment of taxes which exacts from

the owner of the shares of a national bank a larger sum in proportion to their actual value than it does from the owner of other moneyed capital valued in like manner, does tax them at a greater rate within the meaning of the Act of Congress." Where, however, the assessors assess ordinary securities at three fifths of their actual value, and assess bank stock at its full actual value, and such method of unequal assessments is contrary to the Constitution of the State, the court will relieve the stockholders only upon payment by them of such a tax as would have been legal. *Cummings v. Merchants National Bk. of Toledo*, 101 U. S. 153 (1879); *Supervisors v. Stanley*, 105 U. S. 305 (1881). A case similar to the above is reported to have been decided in Cleveland by the Circuit Court of the United States, in November, 1886. When the national bank stock is assessed too low, the fact that another bank is assessed still lower will not invalidate the tax against the former. *People v. Assessors, &c.*, 2 Hun, 583 (1874). In the recent case, *First Natl. Bk. of Toledo v. Treasurer*, 25 Fed. Rep. 749 (1885), where ordinary moneyed capital was assessed at six tenths of its actual value, while shares in national banks was assessed at a higher proportion of the real value, the collection thereof was enjoined, upon the complainant paying the tax admitted to be due.

§ 572. *The bank may bring suit to restrain illegal tax on its stockholders.*—There has been some doubt as to whether a national bank could bring suit to restrain an illegal tax on its stockholders. Ordinarily a corporation cannot do so. Each stockholder must protect his own interests. But where, as in the case of national banks, the tax is paid by the bank itself and collected by it from its stockholders, if the latter refuse to pay the bank or recognize its payment as legal, many suits would result. Accordingly, in order to avoid a multiplicity of suits, it is now well established that the bank itself may file a bill in equity to prevent and enjoin the collection of an illegal tax on its stockholders.¹

¹ *City Natl. Bk. v. City of Paducah*, 2 Flippin, 61 (1877), where the court says: "The bank is so far the trustee of the stockholders, and the custodian of the dividends, that it is entitled to maintain the bill. It might be subjected to great annoyance by stockholders who denied the legality of the tax, and gave the bank notice that it would pay at the peril of being sued by them. It is certainly no hardship to permit the whole question to be litigated in a single action." This case holds also that an injunction against the collection of the illegal tax will be granted. In general, see, also *Albany City Natl. Bk. v. Maher*, 20 Blatch. 341 (1882); *North Ward Natl. Bk. v. Newark*, 40 N. J. L. 558 (1878). *Cf. Dows v. City of Chicago*, 11 Wall. 108; *Tappan v. Merchants Natl. Bk.* 19 Wall. 490; *Pelton v. Natl. Bk.* 101 U. S. 143; *Cum-*

mings v. Natl. Bk., 101 U. S. 153. *Contra*, *First Natl. Bk. of Hannibal v. Meredith*, 44 Mo. 500. See also *Union Natl. Bk. v. Chicago*, 3 Biss. 82. The same rule does not apply to a corporation which brings suit to prevent the levy upon and sale of a non-resident stockholder's stocks for non-payment of his tax. *Waseca County Bk. v. McKenna*, 32 Minn. 468 (1884); *The case of Farmers Natl. Bk. v. Cook*, 32 N. J. L. 347 (1867), denies the right of the bank to bring the action, and says, "The corporation is not the agent of the stockholders for any such purpose." It is clear, where shares of stock are sold under a tax warrant, that the corporation is not obliged to oppose the sale. *McNeal v. Mechanics Building, &c., Assn.*, 12 Am. & Eng. Corp. Cas. 131 (N. J. 1885).

CHAPTER XXXV.

FORMS OF ACTIONS AND MEASURE OF DAMAGES WHERE A STOCKHOLDER HAS BEEN DEPRIVED OF HIS STOCK.

<p>§ 573. Pleading and practice in general in actions relative to stock.</p> <p>574. Assumpsit.</p> <p>575. Trespass on the case.</p> <p>576. Trover.</p> <p>577. Detinue and replevin.</p> <p>578. Money had and received.</p> <p>579. Bill in equity.</p> <p>580. Special action on the case.</p> <p>581. The measure of damages. (a) The first rule.</p>	<p>§ 582. (b) The second rule.</p> <p>583. (c) The third rule.</p> <p>584. Interest, dividends, and accretions.</p> <p>585. Special damages.</p> <p>586. Nominal damages.</p> <p>587. In actions between stock-brokers and their customers. (a) Actions against the broker.</p> <p>588. (b) Actions against the customer.</p>
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§ 573. *Pleading and practice in general in actions relative to stock.*—When an owner of stock who is out of possession brings an action for its recovery, or for the recovery of the certificate, or for damages for the detention or conversion of either the stock or the certificate, it is important to determine what action will lie, in what court the action is to be prosecuted, and what is the measure of damages. Similar questions arise when suits are brought for breach of contract to subscribe for stock, or of contracts to sell and convey stock. There are certain well settled rules as to the form of the action in these cases, which are deduced from the older common law practice and pleading. These rules, even in the Code States, where forms of action are little regarded, and where the old actions have been abolished in name, are still at least partially applicable. Some knowledge, therefore, of the procedure at common law in stock cases is necessary in order to frame pleadings correctly under the modern codes of procedure, since, although the form of the action may have been changed and the name abandoned, the substance of it remains and is material in the modern practice.

§ 574. *Assumpsit.*—An action of assumpsit, or *indebitatus assumpsit* at common law, lies against a corporation for unjustly refusing to register a transfer, or for refusing to issue a certificate

to one entitled to it.¹ So also assumpsit lies for breach of contract to return borrowed bank stock on demand.² But *mandamus* is not a proper remedy in these cases, and it will not lie to compel a corporation to transfer.³

§ 575. *Trespass on the case*.—An action of trespass, or an action of trespass on the case, may also be brought against the corporation for a denial to a stockholder of a certificate of stock,⁴ and an action on the case lies for a conversion of shares of stock.⁵

§ 576. *Trover*.—It is a very generally accepted rule that trover will lie for the conversion of shares of stock.⁶ This is the

¹ *The King v. Bank of England*, Doug. 524 (1780); *Kortright v. Buffalo Commercial Bank*, 20 Wend. 90 (1838); *Arnold v. Suffolk Bank*, 27 Barb. 424 (1857); *Wyman v. American Powder Co.*, 8 Cush. 168 (1851); *Sargent v. Franklin Ins. Co.*, 8 Pick. 90 (1829); *Hayden v. Middlesex Turnpike Co.*, 10 Mass. 397 (1818); *Pinkerton v. Manchester, &c. R. R. Co.*, 42 N. H. 424 (1861); *Hill v. Pine River Bank*, 45 Id. 300 (1864). *Cf.* *Foster v. Essex Bank*, 17 Mass. 479 (1821); *Eastern R. R. Co. v. Benedict*, 10 Gray, 212 (1857).

² *McKenney v. Haines*, 63 Me. 74 (1873).

³ *Freon v. Carriage Co.*, 42 Ohio St. 80 (1884); *Gray v. Portland Bank*, 3 Mass. 364, 381 (1807); *The King v. The Bank of England*, Doug. 524 (1780), by Lord Mansfield. *Cf.* *Curry v. Scott*, 54 Penn. St. 270, 276 (1867). See § 390.

⁴ *Bank of Ireland v. Trustees of Evans' Charities*, 5 H. of L. Cas. 389 (1855); *The King v. Bank of England*, Doug. 524 (1780); *Davis v. Bank of England*, 2 Bing. 393 (1824); *Coles v. Bank of England*, 10 Ad. & Ellis, 437 (1839); *Gray v. Portland Bank*, 3 Mass. 364, 381 (1807); *North American Building Association v. Sutton*, 35 Penn. St. 463 (1860); *Webster v. Grand Trunk Ry. Co.*, 3 Lower Can. Jur. 148 (1859); s. c. 2 Id. 291 (construing the judicature act, 12 Vict. ch. 38, § 87); *Protection Life Ins. Co. v. Osgood*, 93 Ill. 69 (1879); *Baker v. Wasson*, 53 Texas, 150 (1880); *Smith v. Poor*, 40 Me. 415 (1855); *Catchpole v. Ambergate, &c. Ry. Co.*, 1 Ellis & B. 111 (1852); *Daly v. Thompson, Secty. &c. of the Anti-Dry-Rot Co.*, 10 Mees. & W. 309 (1842). *Cf.* *Swan v. North British Australasian Co.*, 7 Hurl. & N. 603 (1862);

Kortright v. Buffalo Commercial Bank, 20 Wend. 90 (1838). Tort with a count in contract for conversion by refusal to transfer. *Bond v. Mount Hope Iron Co.*, 99 Mass. 505 (1868).

⁵ *Daggett v. Davis*, 53 Mich. 35 (1884); *Ayres v. French*, 41 Conn. 142 (1874); *Bank of America v. McNeil*, 10 Bush, 54; *Parsons v. Martin*, 11 Gray, 111 (1858); *Boylan v. Huguet*, 8 Nev. 345 (1873). Although a stockholder whose shares have been duly transferred on the corporate books as security for a debt, may not have such legal title as will enable him to maintain trover against the pledgee for an unauthorized sale, he may maintain a special action on the case and a count in case may be added to the complaint in trover by amendment. *Nabring v. Bank of Mobile*, 58 Ala. 204 (1877).

⁶ *Payne v. Elliot*, 54 Cal. 339 (1880); *Kuhn v. McAllister*, 1 Utah 273 (1875); s. c. 96 U. S. 87 (1877); *Bank of America v. McNeil*, 10 Bush, 54; *Boylan v. Huguet*, 8 Nev. 345 (1873); *Nabring v. Bank of Mobile*, 58 Ala. 204 (1877); *Morton v. Preston*, 18 Mich. 60 (1869); *Jarvis v. Rogers*, 15 Mass. 389 (1810), a case where trover was held to lie for the value of Mississippi scrip, representing 150,000 acres of land; *Anderson v. Nicholas*, 28 N. Y. 600 (1864); *Freeman v. Harwood*, 49 Me. 195 (1859); *Ayres v. French*, 41 Conn. 142 (1874); *Connor v. Hillier*, 11 Rich. Law, 193 (1857); *Sturges v. Keith*, 57 Ill. 451 (1870); *Budd v. Multnomah Street R. R. Co.*, 12 Oregon, 271; s. c. 22 Am. & Eng. R. R. Cas. 27 (1885). *Cf.* *Atkins v. Gamble*, 42 Cal. 86, 100 (1871); *Maryland Fire Ins. Co. v. Dalrymple*, 25 Md. 242, 267 (1866).

favorite remedy when the shareholder has been unjustly deprived of his stock, and it is nowhere denied, except in Pennsylvania,¹ that this form of action is proper. But even there, for the conversion of a certificate of stock, trover will lie.² For the maintenance of the action of trover there must be title in the plaintiff to the subject of the action, and an actual conversion by the defendant. If either of these elements is wanting, the action will not lie. Thus, trover will not lie for the conversion of a certificate where the title to the shares is divested.³ Where several shareholders mutually agree to contribute a number of shares each, to be sold for the benefit of the corporation, one of them cannot, after the rest have contributed their proportion, refuse to allow his shares to be sold, as agreed, and if the corporation takes them under the agreement and sells them, he cannot have an action of trover.⁴ And upon the other hand, withholding possession of a certificate of stock cannot amount to a conversion of the stock itself, so long as the certificate is not indorsed, but it may amount to a technical conversion of the certificate.⁵ It is well established that a refusal of a corporation to register a transfer in the name of one entitled to the stock is a conversion of the shares.⁶ And likewise a failure or refusal by the corporation to issue a certificate to an original subscriber, when, by the terms of the contract of subscription, it ought to be issued, may be treated as a conversion.⁷ So also a failure to deliver stock according to a contract for delivery,⁸ or to return borrowed stock on demand, or

¹ In Pennsylvania it is held that trover will not lie for the conversion of a share of stock. *Sewall v. Lancaster Bk.*, 17 Serg. & R. 285 (1828); *Neiler v. Kelley*, 69 Penn. St. 403 (1871).

² *Biddle v. Bayard*, 13 Penn. St. 150 (1850). *Cf. Aull v. Colket*, 2 Week. Notes Cas. 322 (1875). So in Michigan. *Daggett v. Davis*, 53 Mich. 35 (1884).

³ *Broadbent v. Farley*, 12 C. B. (N. S.) 214 (1862).

⁴ *Conrad v. LaRue*, 52 Mich. 83 (1883).

⁵ *Daggett v. Davis*, 53 Mich. 35 (1884). *Cf. Morton v. Preston*, 18 Id. 60 (1869). Where an administrator sells stock pledged to the deceased in his lifetime as security for a loan of money, and receives the proceeds and properly accounts to the estate, this is not a conversion of the shares, and the pledgor cannot have an action of trover. If any action lies, it is

for money had and received. *Von Schmidt v. Bourn*, 50 Cal. 616 (1875). For an example of an insufficient complaint in trover for shares, in that there was no sufficient averment of a conversion, or of facts from which a conversion might be inferred, see *Edwards v. Sonoma Valley Bank*, 59 Cal. 136 (1881).

⁶ *North America Building Assoc. v. Sutton*, 35 Penn. St. 463 (1860); *West Branch, &c. Canal Co.'s Appeal*, 81* Penn. St. 19 (1870); *Baltimore City, &c. Ry. Co. v. Sewell*, 35 Md. 238 (1871); *McMurrich v. Bond Head Harbour Co.*, 9 Upp. Can. (Q. B.) 333 (1852).

⁷ See § 71.

⁸ *Huntington, &c. Coal Co. v. English*, 86 Penn. St. 247 (1878); *North v. Phillips*, 89 Id. 250 (1879); *Noonan v. Ilsley*, 17 Wis. 314 (1863); *Pinkerton v. Manchester, &c. R. R. Co.*, 42 N. H. 424 (1861).

at the time when, by agreement, it ought to be returned,¹ and an unauthorized sale of stock by a pledgee in violation of the terms of the contract of bailment,² or by a broker in violation of his contract,³ are examples of conversion of stock. In a late case in Oregon it is said that any interference subversive of the right of the owner of stock to enjoy and control it, is a conversion.⁴ In New York, a transferee may try his right to registry in an action for dividends,⁵ but not after commencing an action for conversion.⁶ Where there are conflicting interests in and contending claimants for the same stock, the corporation is not liable for conversion at the suit of one of them in tort, because it may refuse to transfer, pending the contest between the claimants.⁷

§ 577. *Detinue and replevin*.—The common law action of detinue will lie for the recovery of a certificate of stock unlawfully detained.⁸ In this action the judgment is conditional, either to restore the thing detained, or pay the value and damages for the detention. The more modern action of replevin, or its equivalent, will doubtless lie for the recovery of a certificate, as for any other tangible personal property.

§ 578. *Money had and received*.—A pledgor, whose stock has been wrongfully sold by the pledgee, in violation of the contract of bailment, may have an action against the pledgee for money had and received.⁹

¹ McKenney v. Haines, 63 Me. 74 (1873); Fosdick v. Greene, 27 Ohio St. 484 (1875); Forrest v. Elwes, 4 Ves. 492 (1799).

² Maryland Fire Ins. Co. v. Dalrymple, 25 Md. 242, 267 (1866); Freeman v. Harwood, 49 Me. 135 (1859); Fisher v. Brown, 104 Mass. 259 (1870).

³ Colt v. Owens, 90 N. Y. 368 (1882); Harris v. Tumbridge, 83 Id. 92 (1880); Sadler v. Lee, 6 Beav. 324 (1843). But the sale of stock held in pledge is not a conversion when upon redemption the pledgee restores similar certificates and has been at all times ready to do so. Thompson v. Toland, 48 Cal. 99 (1874).

⁴ Budd v. Multnomah St. Ry. Co., 12 Oregon, 271 (1885).

⁵ Robinson v. National Bank of New Berne, 95 N. Y. 637 (1884).

⁶ Hughes v. Vermont Copper Mining Co., 72 N. Y. 207 (1878).

⁷ National Bank of New London v. Lake Shore, &c. R. R. Co., 21 Ohio St.

221, 232 (1871). In trover the goods ought to be set out with some degree of certainty of description, but the same certainty is not required as in detinue and replevin, damages being recovered in trover, where the very articles in detinue and replevin. Neiler v. Kelley, 69 Penn. St. 403 (1871).

⁸ Williams v. Archer, 5 C. B. 318 (1847); s. c. 5 Railway & Canal Cas. 289, where it was held that detinue lay to recover 250 scrip certificates; Peters v. Heywood, Cro. Jac. 682 (21 Jac. 1, 1624), where detinue was allowed for a bond detained.

⁹ Von Schmidt v. Bourn, 50 Cal. 616 (1875); Marsh v. Keating, 1 Bing. (N. C.) 198 (1834). Cf. Jones v. Brinley, 1 East, 1 (1800); The King v. Churchwardens, &c., of the Parish of St. John Maddermarket, 6 Id. 182 (1805). In an old case a contrary rule is laid down. Nightingale v. Devisme, 5 Burr. 2589 (1770).

§ 579. *Bill in equity*.—A bill in equity may be maintained by a *bona fide* purchaser of stock, against the corporation to compel a transfer of the stock upon the corporate books.¹ So, also, a pledgor may have a bill in equity to redeem shares which have been wrongfully sold by the pledgee.²

§ 580. *Special action on the case*.—In many jurisdictions, particularly in those States whose codes of procedure have been modelled more or less after that of New York State, the form of the action in these cases is not material. Accordingly, it will be found that, in these States, there is in general but one form of action by which the plaintiff may equally seek to recover damages for the conversion of his stock, or to compel the corporation to register a transfer to himself, or to have the certificate delivered up, or for any other appropriate relief. It is, however, necessary, in making the allegations, to keep in mind the distinctions which the pleaders at common law observed between the different forms of actions. The modern action, under the codes of procedure, is essentially a special action on the case, wherein the plaintiff in his pleading sets out distinctly his cause of action, and details his grievance without reference to whether the form of his action is *assumpsit* or *case* on the one hand; or *trover*, *detinue*, or *trespass*, on the other.³

¹ *Cushman v. Thayer Mfg. Co.*, 76 N. 365 (1879); *Middlebrook v. Merchants Bank of New York*, 41 Barb. 481 (1864); s. c. 18 Abb. Prac. 109; 27 How. Prac. 474; affirmed 3 Abb. Ct. of App. Dec. 295 (1866); *Buckmaster v. Consumers Ice Co.*, 5 Daly, 313 (1874); *Pollock v. National Bank*, 7 N. Y. 274 (1852); *Loring v. Brodie*, 134 Mass. 453; *Isigi v. Chicago, &c., R. R. Co.*, 129 Mass. 46 (1880); *Conyngnam's Appeal*, 57 Penn. St. 474; *Ashby v. Blackwell*, Amb. 503 (1765). Cf. *Purchase v. New York Exchange Bank*, 3 Robert. (N. Y. Super. Ct.) 164; *White v. Schuyler*, 1 Abb. Prac. (N. S.) 300; *Seymour v. Delancy*, 6 Johns. Chan. 222; s. c. 3 Cowen, 445; *Commercial Bank of Buffalo v. Kortright*, 22 Wend. 348 [the dissenting opinion of the Chancellor] (1839). See § 391.

² *Fowle v. Ward*, 113 Mass. 548 (1873); s. c. 18 Am. Rep. 534. In this case it is held that the true measure of damages is the value of the stock at the time of filing the bill.

³ *Brisbane v. Delaware, &c., R. R. Co.*, 94 N. Y. 204 (1883); *Burrall v. Bushwick R. R. Co.*, 75 Id. 211 (1878). Cf. *Tackerson v. Chapin*, 52 N. Y. Super. Ct. 16 (1885). In Nevada, there is a statutory action of claim and delivery. *Bercich v. Marye*, 9 Nev. 312 (1874). See *Webster v. Grand Trunk Ry. of Canada*, 3 Lower Can. Jur. 148 (1859); s. c. 2 Id. 291, for a construction of that provision of the Judicature Act [12 Vict. ch. 38, § 87] which governs actions of this nature in the Canadian provinces. In *Kuhn v. McAllister*, 1 Utah, 275 (1875), it is held that the language used in the pleadings in these actions is not material, or that the language is that of one form of action or another, or of no form, but that the question is whether the facts entitle the plaintiff to recover. A declaration in an action for the wrongful conversion of the shares of the capital stock of a corporation is sufficient for the purposes of pleading, if it states the ultimate facts to be proven. The circumstances which

§ 581. *The measure of damages.*—(a.) *The first rule.*—Great difficulty has been experienced in determining what shall be the measure of damages for the conversion of stock. As the manner and conditions of the conversion vary, so also will the measure of damages vary, from nominal damages to the highest value of the stock with dividends and interest, and also any special damages which the plaintiff can establish. In general, the courts incline to the rule that the true measure of damages is the value of the stock at the time of the conversion,¹ or a reasonable time after.² By the term the value of the stock is usually to be understood the market value.³ But the fact that the business of the corporation is very profitable, and that its shares of stock have no known market value, or are greatly enhanced by the good will of a growing business, will not vary the

tend to prove that fact can be used for the purpose of evidence; but they have no place in the pleadings. *McAllister v. Kuhn*, 96 U. S. 87 (1877); affirming *Kuhn v. McAllister*, 1 Utah, 275 (1875). As to a misjoinder of causes of action under the California Code, where the plaintiff sues to recover certain stock, see *Johnson v. Kirby*, 65 Cal. 482 (1884). Upon the question of what is, in New York, a sufficient pleading in an action to compel delivery of stock, see *Burrall v. Bushwick R. R. Co.*, 75 N. Y. 211 (1878).

¹ *In re Bahia & San Francisco Ry. Co.*, 3 Q. B. 584 (1868); *Williams v. Archer*, 5 Rail. & Canal Cas. 289 (1847); s. c. 5 C. B. 318. 17 L. J. (C. P.) 82; *Tempest v. Kilner*, 3 C. B. 249 (1846); *Shaw v. Holland*, 15 Mees. & W. 136 (1846); *Pott v. Flather*, 5 Ry. & Canal Cas. 85 (1847); *Davidson v. Tulloch*, 6 Jur. (N. S.) 543 (1860); *Wells v. Abernethy*, 5 Conn. 222, 227 (1824); *O'Meara v. North American Mining Co.*, 2 Nev. 112 (1866); *Baker v. Drake*, 53 N. Y. 211 (1878); s. c., 66 N. Y. 518 (1876); *Colt v. Owens*, 90 N. Y. 368 (1882); *Gruman v. Smith*, 81 Id. 25 (1880); *Ormsby v. Vermont Copper Mining Co.*, 56 Id. 623 (1874); *Pinkerton v. Manchester, &c., R. R. Co.*, 42 N. H. 424; *McKenney v. Haines*, 63 Me. 74 (1873); *Sturges v. Keith*, 57 Ill. 451 (1870); *Noonan v. Ilsley*, 17 Wis. 314 (1863); *Bull v. Douglas*, 4 Munf. (Va.) 303 (1814); *Enders v. Board of Public Works*, 1 Gratt. 334 (1845); *White v. Salisbury*, 33 Mo. 150 (1862); *Connor v. Hillier*, 11 Rich. Law, 193 (1857); *Nabring v. Bank of*

Mobile, 58 Ala. 204; *Eastern R. R. Co. v. Benedict*, 10 Gray, 212; *Boylan v. Huguet*, 8 Nev. 345 (1873); *Bercich v. Marrye*, 9 Id. 312 (1874); *Sargent v. Franklin Ins. Co.*, 8 Pick. 90 (1829); *Fisher v. Brown*, 104 Mass. 259 (1870); *Wyman v. American Powder Co.*, 8 Cush. 168; *North v. Phillips*, 89 Penn. St. 250 (1879); *Huntington, &c., Coal Co. v. English*, 86 Id. 247 (1878); *Neiler v. Kelley*, 69 Id. 403 (1871); *Randall v. Albany City National Bank*, 1 N. Y. State Rep. 692 (Sept., 1886); *Douglas v. Merceles*, 25 N. J. Eq. 144 (1874). See also *Eicholz v. Fox*, 12 Phila. 382 (1878); *Larrabee v. Badger*, 45 Ill. 440 (1867); *Barned v. Hamilton*, 2 Rail. & Canal Cas. 624 (1841); *Blyth v. Carpenter*, L. R. 2 Eq. 501 (1866).

² *Colt v. Owens*, 90 N. Y. 368 (1882); *Douglas v. Merceles*, 25 N. J. Eq. 144 (1874). Upon what is reasonable time herein in transactions on the stock exchanges, see *Stewart v. Cauty*, 8 Mees. & W. 160 (1841); *Field v. Lelean*, 6 Hurl. & N. 617.

³ By the "market value of stock" is meant the actual price at which it is commonly sold. That price may be fixed by sales of the stock in market at or about a given time. If no sales can be shown on the precise day, recourse may be had to sales before or after the day, and for that inquiry a reasonable range in point of time is allowable. *Douglas v. Merceles*, 25 N. J. Eq. 144 (1874). Cf. *Stewart v. Cauty*, 8 Mees. & W. 160 (1841); *Sturges v. Keith*, 57 Ill. 451 (1870); *Seymour v. Ives*, 46 Conn. 109 (1878).

rule where the actual value is ascertainable in an action to recover damages.¹ The question of what was the market value at the time of the conversion is generally a question for the jury,² and it may be shown by tables of prices current, published in the newspapers or otherwise at the time of the conversion, and these may be read in evidence.³ Again, it is not always entirely clear at what time the conversion was consummated, particularly when the question arises between pledgor and pledgee, vendor and vendee, or shareholder and the corporation.

In general, however, a conversion for which the owner of the stock may have an action, arises whenever the stockholder, being entitled to the immediate possession or delivery of the stock or the certificate, makes a demand for it, which is refused. Accordingly, in this class of cases the measure of damages is the value of stock on the day of the demand and refusal.⁴

¹ "In actions for conversion of personal property, such as these shares are, the damages are not limited to the market value of the stock. Its actual value to be determined under all the circumstances, such as the dividend-making capacity, the good will, &c., &c., is the measure of damages." *Freon v. Carriage Co.*, 42 Ohio St. 30, 38 (1884). Not the nominal, but the true value of the shares is what the plaintiff is entitled to recover. *Bull v. Douglas*, 4 Munf. (Va.) 303 (1814); *Enders v. Board of Public Works*, 1 Gratt. 364 (1846).

² 1 Sedgwick on Damages (7th ed.), 585, and cases cited. *Dos Passos on Stock-brokers*, 801. See *Cameron v. Durkheim*, 55 N. Y. 425 (1874); *Fowler v. New York Gold Exchange Bank*, 67 Id. 138 (1876); *Harris v. Tumbridge*, 83 Id. 92 (1880).

³ *Cliquot's Champagne*, 3 Wall. 114 (1865). In this case it is said that such price lists as were printed and published at the time of the prices in dispute, and meant to be relied on at that time in commercial transactions, may be submitted to the jury as "throwing light" on the matter, as "some guide to candid men," and for their "consideration." s. r., *Whelan v. Lynch*, 60 N. Y. 469 (1875).

⁴ So when stock, held as collateral, is improperly sold by the pledgee, the value on the day when the pledgor pays his debt and demands his stock is to be taken. *Fisher v. Brown*, 104 Mass. 259 (1870). In *Freeman v. Harwood*, 49 Me. 195 (1859), shares of stock standing in the

name of the defendant as collateral security for a debt which had been paid, were sold for non-payment of an assessment, and bought by defendant. It was held that the defendant was liable in *trover* for the value of the shares at the time of the sale, with interest, and all dividends received thereon, deducting the amount of the assessment and the expenses of the sale. In *Sturges v. Keith*, 57 Ill. 451 (1870), it is held that where the demand and refusal constitute the conversion, or afford presumptive evidence of it, the date of such demand and refusal is the proper time for estimating the value. Again, where the corporation wrongfully refuses to register a transfer and to issue a certificate, the measure of damages is the value of the stock on the day when the transfer was demanded and refused. *Wyman v. American Powder Co.*, 8 Cush. 168 (1851); *Eastern R. R. Co. v. Benedict*, 10 Gray, 212 (1857); *West Branch, &c., Canal Company's Appeal*, 81* Penn. St. 19 (1870); *Baltimore City, &c., R. R. Co. v. Sewell*, 35 Md. 238 (1871). *McMurrich v. Bond Head Harbor Co.*, 9 Up. Can. (Q. B.) 333 (1852), where it is said that while the rule, as announced above, is the proper one, when the jury allows a larger sum, the question of the measure of damages not having been pressed at the argument, the court will not reduce the verdict. So also where there is a failure to return borrowed stock on demand, or according to the terms of the bailment, the value on the day of demand, or on the day when the stock ought by contract

§ 582. (b.) *The second rule.*—In another line of cases the true measure of damages in these actions is said to be the value of the stock on the day of the trial.¹ In an English case it is said that this is a sound rule in the ordinary cases of conversion of stock, but that in cases of failure to deliver stock the true measure of damages is the value when the demand is made and refused.² This rule has, however, found little favor, and there is believed to be no sound reason for its adoption.

§ 583. (c.) *The third rule.*—It has been held, in still another class of decisions, that the measure of damages for the conversion of stock is the highest market value of the stock between the date of the conversion and the day of the trial. This is the rule in California in some cases.³ So also in South Carolina,⁴ Georgia,⁵ and it was formerly the rule in New York⁶ and Pennsylvania.⁷

to have been returned, is the measure of damages. *McKenney v. Haines*, 63 Me. 74 (1873); *Fosdick v. Greene*, 27 Ohio St. 484 (1875); s. c., 22 Am. Rep. 328; *McArthur v. Seaforth*, 2 Taunt. 257; *Day v. Perkins*, 2 Sandf. Chan. 359. *Cf.* *Cortelyou v. Lansing*, 2 Caines' Cas. in Error, 200 (1805); *West v. Wentworth*, 3 Cowen, 82; *Clark v. Pinney*, 7 Id. 681; *Wilson v. Matthews*, 24 Barb. 295; 2 *Sedgwick on Damages* (7th ed.), 141, 365, n. In an old case where borrowed stock was not returned, the plaintiff was allowed to recover the value at the time of the transfer to the borrower, no account being taken of an increase in value. *Forrest v. Elwes*, 4 Ves. 492 (1799). *Acc.* *McKenney v. Haines*, 63 Me. 74 (1873). Upon a failure to deliver stock according to contract or on demand, the value at the time of the demand is the value to be taken. *Noonan v. Ilsley*, 17 Wis. 314 (1863); *Pinkerton v. Manchester, &c.*, R. R. Co., 42 N. H. 424 (1861); *North v. Phillips*, 89 Penn. St. 250 (1879); *Huntington, &c., Coal Co. v. English*, 86 Id. 247 (1878). *Cf.* *Pott v. Flather*, 5 Rail. & Canal Cas. 85 (1847); *Barned v. Hamilton*, 2 Id. 624 (1841); *Shaw v. Holland*, 4 Id. 150 (1846); s. c., 15 Mees. & W. 136; *Tempest v. Kilner*, 2 C. B. 300; s. c., 3 Id. 249; *Gainsford v. Carroll*, 2 Barn. & C. 624.

¹ *Owen v. Routh*, 14 C. B. 327 (1854); *Shepherd v. Johnson*, 2 East, 211; *Berchich v. Marye*, 9 Nev. 312 (1874). *Cf.* *Williams v. Archer*, 5 C. B. 318 (1847); s. c., 5 Rail. & Canal Cas. 289; 17 L. J. (C. P.) 82; and see *Wilson v. Little*, 2 N. Y. 443, 450 (1849), wherein there is a

quere as to whether this may not be the better rule. In *Fowle v. Ward*, 118 Mass. 548; s. c., 18 Am. Rep. 534 (1873), it is held that the measure of damages is the value of the stock upon the day when the bill in equity is filed, it being an equitable action by a pledgor against a pledgee.

² *Shaw v. Holland*, 15 Mees. & W. 136, 145 (1846); s. c., 4 Rail. & Canal Cases, 150; 15 L. J. Exch. 87.

³ Code of California, § 3336, is as follows: "The detriment caused by the wrongful conversion of personal property is presumed to be: 1. The value of the property at the time of the conversion, with interest from that time; or where the action has been prosecuted with reasonable diligence, the highest market value of the property at any time between the conversion and the verdict, without interest, at the option of the injured party." This is held to apply to the conversion of shares of stock. *Fromm v. Sierra Nevada Silver Mining Co.*, 61 Cal. 629 (1882); *Dent v. Holbrook*, 54 Id. 145 (1880). *Cf.* *Thompson v. Toland*, 48 Cal. 99 (1874).

⁴ *Kid v. Mitchell*, 1 Nott & McCord, 334.

⁵ *Central R. R. & Banking Co. v. Atlantic, &c.*, R. R. Co., 50 Ga. 444.

⁶ *Markham v. Jaudon*, 41 N. Y. 235 (1869); *Romaine v. Van Allen*, 26 Id. 309 (1863).

⁷ *Bank of Montgomery v. Reese*, 26 Penn. St. 143 (1856); *Musgrave v. Beckendorff*, 53 Id. 310 (1866); *Reitenbaugh v. Ludwick*, 31 Id. 131, 141 (1858).

The courts of the two latter States have, however, in later cases, wholly receded from this position, and in both the rule is now established, that in general, in such actions, the measure of damages is not the highest price of the stock, but the value at the date of the conversion.¹

§ 584. *Interest, dividends, and accretions.*—It is settled law that, in addition to the value of the stock at the date of conversion, the plaintiff may recover legal interest upon such valuation from the date of the conversion to the day of the trial. It follows, as of course, that if the plaintiff has been damaged in an ascertained sum, he may, in an action for damages, recover not only that sum, but interest thereon, for the time during which he has been wrongfully deprived of his stock.² In addition to interest, the plaintiff may recover also all accretions to the property made during the time when he was deprived of it. He is, therefore, entitled to judgment for all dividends paid upon the stock between the date of the conversion and the day of the trial.³ The reason why the plaintiff recovers dividends in addition to the value of the stock and interest, is probably this. It often occurs that the dividends involved were earned, wholly or in part, before

¹ *North v. Phillips*, 89 Penn. St. 250 (1879); *Huntington, &c., Coal Co. v. English*, 86 Id. 247 (1878); *Work v. Bennett*, 70 Id. 484 (1872); *Neiler v. Kelley*, 69 Id. 403 (1871). Cf. *Wilson v. Whittaker*, 49 Id. 114 (1865). So also in the later New York cases. *Baker v. Drake*, 53 N. Y. 211 (1873); s. c., 66 N. Y. 518 (1876); *White v. Smith*, 54 Id. 522 (1874); *Harris v. Tumbidge*, 83 Id. 92 (1880); *Colt v. Owens*, 90 Id. 368 (1882); *Randall v. Albany City National Bank*, 1 N. Y. State Rep. 592 (Sept., 1886). Cf. *Suydam v. Jenkins*, 3 Sandf. Super. Ct. 614 (1850); *Matthews v. Coe*, 49 N. Y. 57 (1872); *Bryan v. Baldwin*, 52 Id. 236 (1873). See also *Seymour v. Ives*, 46 Conn. 109 (1878); *McGuffey v. Humes* (Sup. Ct. Tenn. Sept. 1886), 1 South-west. Rep. 506.

² *O'Meara v. North American Mining Co.*, 2 Nev. 112 (1866); *Boylan v. Huguet*, 8 Id. 345 (1873); *Fisher v. Brown*, 104 Mass. 259 (1870); *Sargent v. Franklin Ins. Co.*, 8 Pick. 90 (1829); *Seymour v. Ives*, 46 Conn. 109 (1878); *McKenney v. Haines*, 63 Me. 74 (1873); *Freeman v. Harwood*, 49 Id. 195 (1859); *Ormsby v. Vermont Copper Mining Co.*, 56 N. Y.

623 (1874); *White v. Smith*, 54 Id. 522 (1874); *Sturges v. Keith*, 57 Ill. 451 (1870); *Baltimore City, &c., Ry. Co. v. Sewell*, 35 Md. 238, 257 (1871); *Pinkerton v. Manchester, &c., R. R. Co.*, 42 N. H. 424 (1861); *North v. Phillips*, 89 Penn. St. 250 (1879); *Huntington, &c., Coal Co. v. English*, 86 Id. 247 (1878); *North America Building Assoc. v. Sutton*, 35 Id. 463 (1860); *Noonan v. Ilsley*, 17 Wis. 314 (1863); *Forrest v. Elwes*, 4 Ves. 492 (1799); *In re Bahia & San Francisco Ry. Co.*, 3 Q. B. 584 (1868); *Blyth v. Carpenter*, L. R. 2 Eq. 501 (1866); *McMurrich v. Bond Head Harbor Co.*, 9 Upp. Can. (Q. B.) 333 (1852). In the Civil Code of California, § 3336, interest in these cases is expressly provided for. *Fromm v. Sierra Nevada Silver Mining Co.*, 61 Cal. 629 (1882); 2 *Sedgwick on Damages* (7th ed.), 391.

³ *Bull v. Douglas*, 4 Munf. (Va.) 303 (1814); *Baltimore City, &c., Ry. Co. v. Sewell*, 35 Md. 238 (1871); *Bercich v. Marye*, 9 Nev. 312 (1874); *Bank of Montgomery v. Reese*, 26 Penn. St. 143 (1856). Cf. *Boston, &c., R. R. Co. v. Richardson*, 135 Mass. 473, 477 (1883).

the conversion, though declared and paid after the conversion. The market value will not in such cases, as a rule, represent the true value, including the dividends, and, therefore, a judgment for the mere value of the shares and interest would not be adequate compensation for the conversion.

§ 585. *Special damages*.—The plaintiff may also recover any special damages which legitimately arise out of matters in existence at the date of the conversion, and which he has sustained by reason of the detention of his stock.¹ This is the general rule, but it seems that in Connecticut such special damages in *trover*, in cases of conversion of stock, are not favored.²

§ 586. *Nominal damages*.—In certain cases, where the plaintiff has been guilty of laches, or where the stock is of no actual value, or where the stock could, for a reasonable time after the conversion, have been purchased in the market for the same or a lower price, or in any other case where the plaintiff has suffered only a technical conversion without any actual pecuniary loss, only nominal damages can be recovered.³ Thus the

¹ Boylan v. Huguet, 8 Nev. 345 (1873); 2 Sedgwick on Damages (7th ed.), 391; Bodley v. Reynolds, 8 Ad. & El. (N. S.) 779 (1846); Davis v. Oswell, 7 Car. & P. 804 (1837). Where the president of a company issues spurious stock in excess of the amount authorized by law, the measure of damages, in actions by those who take such stocks *bona fide*, is the pecuniary equivalent of such shares, it being impossible to decree an allotment of the shares themselves. Willis v. Fry, 13 Phila. 33 (1879). In an action on the case against a building society, for unjustly refusing to permit a transfer of certain shares of stock held by the plaintiff, the latter may recover the amount paid on the stock, as dues, with interest thereon from the time of the several payments. North America Building Association v. Sutton, 35 Penn. St. 463 (1860). In an action by a corporation against one to whom the corporation has issued a certificate upon a forged power of attorney to transfer, the measure of damages will embrace (a) the costs and expenses incurred by the corporation in defending a suit brought against it by the person whose name was forged; (b) the amount required to replace the stock so unlawfully transferred; (c) dividends which the corpora-

tion was obliged to pay to the one whose name was forged. Barton, &c., R. R. Co. v. Richardson, 135 Mass. 473, 477 (1883). Bankers of trustees wrongfully sold out stock, and applied the proceeds to their own purposes. The measure of their liability is the amount paid in replacing the stock. Sadler v. Lee, 6 Beav. 324 (1848). As to damages in cases of trusts, see Story's Eq. (13 ed.), §§ 1263, 1264: Upon the effect of false and fraudulent representations, on an action for damages, see Tockerson v. Chapin, 52 N. Y. Super. Ct. 16 (1885). It is no defense to such an action that the original conversion was by some one else. Kuhn v. McAllister, 1 Utah, 275 (1875); *s. c. sub nom.*, McAllister v. Kuhn, 96 U. S. 87 (1877).

² Seymour v. Ives, 46 Conn. 109 (1878).

³ Thus where a borrower of shares fails to return them until after the corporation is dissolved, the lender having made no demand during the existence of the company, the measure of damages, in an action to recover the shares, will be the market value of them at the time the course of action accrued, that is at the time of a demand. And if at that time the stock is worthless only nominal damages are recoverable. Fosdick v.

measure of damages for the conversion of a mere certificate of stock cannot be placed at the value of the shares themselves which the certificate represents, if the ownership of the shares is not affected.¹

§ 587. *In actions between stock-brokers and their customers.*—(a.) *Actions against the broker.*—Where a broker buys or sells stock on his customer's account in violation of the terms of his contract, and thereby makes a profit, the customer has his option either to repudiate the transaction altogether and sue for damages, or he may adopt it and claim for himself the benefit made by his agent.² It has been held that where the broker fails to buy according to the instructions of his customer, and the customer suffers a loss by reason of the failure, the object of the purchase being to cover a short sale, the measure of damages is the difference between the price at which the stock was sold short and the market price upon the day when the order was given to the broker to buy in, that is to say, the plaintiff may in such a case recover the profits which he would necessarily have made had his order been properly executed.³ And the rule is the same when

Greene, 27 Ohio St. 484 (1875); s. c. 22 Am. Rep. 328. See *Cameron v. Durkheim*, 55 N. Y. 425 (1874); *Hope v. Lawrence*, 50 Barb. 258. In an action on a contract for the sale of specific stock, which, without the knowledge of the vendor, had already been sold to another by his agent, the plaintiff can recover only nominal damages. *Wilson v. Whitaker*, 49 Penn. St. 114 (1865). *Acc. Skinner v. City of London, &c. Ins. Corporation*, L. R., 14 Q. B. Div. 882 (1885). See *Fowler v. New York Gold Exchange Bank*, 67 N. Y. 138. Where a broker sold stock for his customer without authority, and in violation of an agreement not to sell, and it appeared that, for thirty days after notice was given to the customer of the sale the stock could have been purchased in the market for the price at which it was sold or even for less, it was held, in an action to recover damages, that the customer having had a reasonable time after he was notified of the sale of his stock, to replace it at the same or a lower price, was entitled only to nominal damages. *Colt v. Owens*, 90 N. Y. 368 (1882). *Cf. Randall v. Albany City National Bank*, 1 N. Y. State Rep. 592 (Sept. 1886). See also *McArthur v.*

Seaforth, 2 Taunt. 257. But when the action of the broker is fraudulent the customer may, upon obtaining knowledge of the facts, repudiate the whole transaction and recover back the money paid. *Levy v. Loeb*, 89 N. Y. 386 (1882); reversing s. c. 15 Jones & Spencer, 61. *Cf. Stewart v. Drake*, 46 N. Y. 449 (1871).

¹ *Daggett v. Davies*, 53 Mich. 35 (1884), by Cooley, C. J.

² *Kimber v. Barber*, L. R., 8 Chan. 56; *Marsh v. Keating*, 1 Bing. N. C. 198 (1834); *Taussig v. Hart*, 49 N. Y. 301 (1872); s. c. 58 N. Y. 425 (1874); *Pickering v. Demeritt*, 100 Mass. 416; *Day v. Holmes*, 103 Id. 306.

³ In an action to recover damages, where a firm of stock-brokers sold, for a customer upon his order and for his account, 300 shares of stock, short, at 186, and subsequently, without the customer's order or knowledge, bought in stock to cover the sale, and then, a few days later, the stock having declined several points, the customer ordered them to cover their sale, to which order no attention was paid, it was held that the proper measure of damages was the difference between the price at which the stock was sold short and the market price upon the day

the loss to the customer results from the failure of the broker to sell as instructed, or where the broker sells at an improper or manifestly unfavorable time.¹ Where one has been induced by fraudulent misrepresentations to buy or subscribe for shares of stock, the measure of damages, in an action against the vendor, is the difference between the value of the stock as represented, and the actual value.² And where one, with intent to cheat and defraud, induces another, by false and fraudulent representations, to purchase shares for value which he knows to be worthless, he is liable for the damages sustained, whether the purchase was made from him or from another at his instance.³ Where a broker converts the securities of his customer, the measure of damages is the value at the time of the conversion, with interest to the day of the trial, and past dividends.⁴ This rule is sometimes so modi-

when the order was received to purchase, with interest, deducting commissions, &c. *White v. Smith*, 54 N. Y. 522 (1874).

See *Magee v. Atkinson*, 2 Mees. & W. 440.

¹ In *Harris v. Tumbidge*, 83 N. Y. 92 (1880), it appears that the plaintiff purchased, through the agency of the defendant, a stock option, a privilege known as a "straddle," upon the defendants guarantee that the fluctuations in the stock during the pendency of the contract should amount to eight per cent. On the next day after the purchase defendant sold the stock, short, which resulted in a loss to the plaintiff, who had, at the time of the purchase, authorized defendant, as her agent, to exercise the option. As to the measure of damages, the court say: "An objection is taken to the rule of damages. It is insisted that as plaintiff never gave any directions to 'put' or 'call' the stock, she should not have recovered as if she had. But in the absence of such directions it was defendant's duty, under the circumstances of this case, as we have already said, to have closed the 'straddle' contract by exercising the option at the most favorable time, and to have acted for her in that respect with reasonable care and skill. As he did not do so, she is entitled to recover what she has lost by his neglect, and the price of the stock from day to day during the running of the option having been shown, it was for the jury to determine that amount." Cf. *Speyer v. Colgate*, 4 Hun, 622 (1875).

² *Miller v. Barber*, 66 N. Y. 558, 568

(1876); *Hubbell v. Meigs*, 50 Id. 480, 491 (1872).

³ *Hubbell v. Meigs*, *supra*.

⁴ *Baker v. Drake*, 53 N. Y. 211 (1873); s. c. 66 Id. 518 (1876); *Brass v. Worth*, 40 Barb. 648; *Gruman v. Smith*, 81 N. Y. 25 (1880); *Burridge v. Anthony*, N. Y. Marine Ct. (1880); *Colt v. Owens*, 90 N. Y. 368 (1882); *Randall v. Albany City National Bank*, 1 N. Y. State Rep. 592 (Sept. 1886); *North v. Phillips*, 89 Penn. St. 250 (1879). Cf. *Moody v. Caulk*, 14 Fla. 50; *Kent v. Ginter*, 23 Ind. 1; *Orange, &c., R. R. Co. v. Fulvey*, 17 Gratt. 366; *Jefferson v. Hale*, 31 Ark. 286; *Third National Bank v. Boyd*, 44 Md. 47; *Thomas v. Sternheimer*, 29 Id. 268. The "highest price" rule formerly prevailed in New York. *Markham v. Jaudon*, 41 N. Y. 235 (1869); *Romaine v. Allen*, 26 Id. 309 (1863); *Lawrence v. Maxwell*, 6 Lans. 469; *Nauman v. Caldwell*, 32 N. Y. Super. Ct. 212 (1870). In an action to recover damages for the unlawful conversion of a quantity of grain, it seems that the rule in New York is that the highest price up to the time of the trial is the proper measure of damages. *Lordell v. Stowell*, 51 N. Y. 70 (1872). In this case the court assumes that the rule which applies as to the measure of damages for the conversion of shares of stock is not applicable to a conversion of property other than shares, and that the rule in the text is rather an exception to the general rule as to measure of damages in case of the conversion of other classes of personal property. The same view is

fied as to allow the plaintiff to recover any advance in the price of the stock within a reasonable time after notice of the conversion is brought to him.¹ And what is a reasonable time in such a case is a question for the jury.²

§ 588. (b.) *Actions against the customer.*—It is a well settled rule that if a broker, acting in good faith, and without default, incurs personal loss or damage in the course of transacting the business of his agency, or in following the instructions of his principal, he may recover from the principal full compensation therefor.³ Accordingly, where a broker buys stock upon his customer's order and pays for it, and upon a decline in value the customer refuses to accept it, the broker may recover the price paid by him, and not merely the difference between that price and the market value on the day of his demand.⁴ Where a vendee

taken in an Indiana case. *Kent v. Ginter*, 23 Ind. 1 (1864). See 1 Sedgwick on Damages (7th edition), 578, and note (a). *Cf. Burt v. Dutcher*, 34 N. Y. 493 (1866); *Scott v. Rogers*, 31 Id. 676 (1864); *Devlin v. Pike*, 5 Daly (N. Y.) C. P. 85. In Pennsylvania where one is accountable for stock as trustee, and converts it, he is chargeable with the highest market value. *Reitenbaugh v. Ludwick*, 31 Penn. St. 131 (1858); *North v. Phillips*, 89 Penn. St. 250 (1879). See also *Kid v. Mitchell*, 1 Nott & McCord, 334; *Central, &c., R. R. Co. v. Atlantic, &c., R. R. Co.*, 50 Ga. 444. *Cf. Bates v. Wiles*, 1 Handy (Ohio), 532. In California the Civil Code provides that the measure of damages in the case of a conversion of personal property, shall be the value at conversion, or where the action is brought promptly, the highest market value. Cal. Civil Code, § 3336. The courts have held that this section of the Code applies to the conversion of shares of stock, but they have not worked out a very consistent rule on the subject. In *Douglass v. Craft*, 9 Cal. 562, the "highest value" rule is adopted, but in later cases the court seems to incline toward the modern New York rule. *Hamer v. Hathaway*, 33 Cal. 117; *Page v. Fowler*, 39 Id. 412; *Dent v. Holbrook*, 54 Id. 145 (1880); *Tully v. Tranor*, 53 Id. 274; *Thompson v. Toland*, 48 Id. 99 (1874); *Fromm v. Sierra Nevada Silver Mining Co.*, 61 Cal. 629 (1882). For the measure of damages where a broker converts his customer's securities, and then is unable

by reason of his insolvency to replace them, see *Chamberlain v. Greenleaf*, 4 Abb. New Cas. 92, 178.

¹ *Gruman v. Smith*, 81 N. Y. 25 (1880); *Burridge v. Anthony*, N. Y. Marine Ct. (1880); *Page v. Fowler*, 39 Cal. 412.

² *Baker v. Drake*, 66 N. Y. 518 (1876); *Stevens v. Hurlbut Bank*, 31 Conn. 146; *Stewart v. Cauty*, 8 Mees. & W. 160; *Field v. Lelean*, 6 Hurl. & N. 617. *Cf. Allen v. Dykers*, 3 Hill, 593 (1842).

³ 2 Sedgwick on Damages (7th edition), 86; *Lindley on Partnership* (4th edition), 731 [where the English authorities upon the right of a stock-broker to indemnity from his principal, and the measure of damages in such cases, are collected and fully considered]; citing *Sutton v. Tatham*, 10 Ad. & E. 27; *Bayliffe v. Butterworth*, 1 Exch. 425; *Bowlby v. Bell*, 3 C. B. 284; *Bayley v. Wilhins*, 7 Id. 886; *McEwen v. Woods*, 2 Car. & K. 330; *Taylor v. Stray*, 2 C. B. (N. S.) 175; *Stray v. Russell*, 1 El. & El. 888; *Chapman v. Shepherd*, L. R. 2 C. P. 228; *Biederman v. Stone*, Id. 504; *Mollett v. Robinson*, L. R., 7 H. L. 802; s. c. 7 C. P. 84; 5 C. P. 646; *Pollock v. Stables*, 12 Q. B. 765; *Lacey v. Hill*, 8 Chan. 921; *Dos Passos on Stock Brokers*, 123, 802.

⁴ *Giddings v. Sears*, 103 Mass. 311. *Cf. Field v. Kinnear*, 4 Kan. 476. Where there is a rescission of a contract for the sale of stock, the measure of the damages is the value of the stock at the time and place of the proposed delivery. *White v. Salisbury*, 33 Mo. 150 (1862); *Vance v. Tourne*, 13 La. 225.

refuses to carry out an executory contract for the sale of shares, the measure of damages is the difference in value of the stock at the time of tender and refusal, and at the time the vendee gave notice of his purpose to repudiate.¹

¹ *Barned v. Hamilton*, 2 Rail. & Canal Cas. 624 (1841). *Cf.* *Tempest v. Kilner*, 3 C. B. 249 (1846), and *Stewart v. Cauty*, 8 Mees. & W. 160 (1841), wherein it is held that in such a case the proper measure of damages is the difference of the prices of the shares on the day when they ought to have been accepted, and on the day when they were resold by the vendor, such sale being within a reasonable time. In *Shaw v. Holland*, 15 Mees. & W. 136 (1846), the proper measure of damages is said to be the difference between the contract price and the market price on the day when the contract was broken.

CHAPTER XXXVI.

CORPORATE MEETINGS.—CALLS, TIME, PLACE, AND CLASSES OF MEETINGS.

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| <p>§ 589. Introductory.</p> <p>590. The meeting must be held at the prescribed time, which must be reasonable.</p> <p>591. The place of meeting must be within the State creating the corporation.</p> <p>592. Validity of corporate acts at meetings outside the State.</p> <p>593. By whom meetings are to be called.</p> <p>594. When the stockholders are entitled to notice of corporate meetings.</p> | <p>§ 595. The essential elements of a notice of a meeting are time, place, and business.</p> <p>596. Service of the notice.</p> <p>597. Notice must be served a reasonable time before the meeting.</p> <p>598. The division of meetings into ordinary and extraordinary.</p> <p>599. Waiver of notice.</p> <p>600. Notice is presumed to have been regularly given.</p> <p>601. Adjourned meetings.</p> |
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§ 589. *Introductory.*—The stockholders of a corporation constitute the essential existence and continued life of the corporation itself. They elect its officers, control its general policy, and, within the charter limits, may prolong or dissolve its existence at their pleasure. All these vital powers of the stockholders can be exercised by them only in corporate meetings duly convened and properly organized for the transaction of business. Accordingly, the method of calling together a corporate meeting, the time and place of that meeting, the notice to be given to the stockholders, and the various incidents relative to a proper convening of the members of the corporation, are of great importance. They constitute the subject of this chapter.

§ 590. *The meeting must be held at the prescribed time, which must be reasonable.*—The particular time at which corporate meetings shall be held is often prescribed in the charter, or a statute, or in the by-laws of the corporation. When not so prescribed, it is fixed by the officers who call together the corporate meeting. But, in whatever way it is decided upon, the meeting must be convened at the time decided upon, or within a reason-

able time thereafter.¹ Accordingly, if the meeting is convened before the hour at which it is called, and business is transacted, the proceedings will be invalid.² Under the incorporating acts of some of the States, meetings of incorporators for the purpose of organization, election of directors, &c., may properly be held before the full capital stock is subscribed.³ In general, a court of equity will restrain the directors from fixing the time for an annual meeting at a date when many members are in the country, the purpose being to prevent them from exercising their right to vote.⁴

§ 591. *The place of meeting must be within the State creating the corporation.*—The first and most general rule as to the place where stockholders may hold corporate meetings, is that the place of meeting must be within the limits of the State by which the corporation is created. Inasmuch as stockholders can meet and act in the capacity of stockholders only by virtue of the existence of the corporation, and since the corporation exists only in the State creating it, the power of stockholders to meet

¹ Where a meeting was held by a minority of the stockholders several hours after the time fixed in the notice, and an adjournment made until the following day, at which adjourned meeting, without the knowledge of the other members, an election was held, the election was unfair and invalid. *State of Ohio v. Bonnell*, 35 Ohio St. 10 (1878). But a delay of an hour and five minutes after the time specified in the notice, is not, as a matter of law, an unreasonable delay which will vitiate the proceedings. *South School District v. Blakeslee*, 18 Conn. 227, 235 (1839). In this case the court says: "The presumption of law is that the meeting was holden at a suitable and proper time in the day, and in pursuance of the warning. If the defendant claims that the proceedings were illegal, the burden of proof is upon him. If there was an unreasonable delay in opening the meeting, he must show it. This he has not done by merely proving that there was delay of one hour and five minutes; for there is no law, statute or common, that necessarily requires the meeting to be opened within that time after the hour appointed. Nor has he done it by merely proving that a few persons left, for they may have gone away for the purpose of preventing the meeting from acting. If there were

any particular circumstances which rendered a delay of that length of time unreasonable, the defendants ought to have shown them."

² So where a meeting was called for twelve o'clock, but was called to order and organized fifteen minutes before twelve, it was held to be a surprise and a fraud upon such of the shareholders as were not actually present at that hour, and that in consequence the proceedings were irregular and void. *People v. Albany, &c., R. R. Co.*, 55 Barb. 344 (1869). Where commissioners, after calling a meeting of subscribers, ordered the election postponed, but the subscribers nevertheless refuse to postpone, and proceed with the election, the election is not void, unless, in the opinion of the court, a postponement was clearly necessary. *Hardenburgh v. Farmers & Merchants Bank*, 3 N. J. Eq. 68 (1834). *Quere*, in this case, whether the election might not have been avoided, if any considerable number of the shareholders were deprived of their election franchise by the failure to postpone. *Cf. People v. Batchelor*, 22 N. Y. 128 (1860).

³ *Perkins v. Sanders*, 56 Miss. 738 (1879).

⁴ *Cannon v. Trask*, L. R., 20 Eq. 669 (1875).

and do corporate acts is necessarily bounded by the State lines. It is therefore the settled rule that the acts which are essential to the existence and continuation of the corporation itself, can only be exercised within the bounds of the State, from which the corporation derives its corporate existence. Hence, a meeting of the stockholders of a corporation can only be held in the State which has incorporated the company.¹ Accordingly, it is the rule that no legal organization by the incorporators under a charter granted by one State, can lawfully be affected by their meeting and action in another State.² It is not doubted that a corporation may act by its agents outside of the State which creates it. Thus it may, as of course, make contracts, carry on its proper business, sue and be sued, and acquire and hold property in a foreign State.³ Accordingly, as directors are merely corporate agents, they may lawfully hold meetings in foreign States, and their acts as directors at such meetings are lawful and valid.⁴ Frequently

¹ *Miller v. Ewer*, 27 Me. 509 (1847); *Smith v. Silver Valley Mining Co.*, 64 Md. 85 (1885); s. c. 10 Am. & Eng. Corp. Cas. 1; 54 Am. Rep. 760; *Franco-Texas Land Co. v. Laigle*, 59 Texas, 339; *Ormsby v. Vermont Copper Mining Co.*, 56 N. Y. 623 (1874); *Hilles v. Parrish*, 14 N. J. Eq. 380 (1862). See also *Plimpton v. Bigelow*, 93 N. Y. 592, 598 (1883); *Merrick v. Van Santvoord*, 34 Id. 208, 218 (1866); *Stevens v. Phoenix Ins. Co.*, 41 Id. 149 (1869); *LaFayette Ins. Co. v. French*, 18 How. 404; *Reichwald v. Commercial Hotel Co.*, 106 Ill. 439 (1883); *Farnum v. Blackstone Canal Corporation*, 1 Sumner, 46; *Day v. Newark India Rubber Mfg. Co.*, 1 Blatchf. 628.

"It has, ever since the decision of the Supreme Court, in the case of *The Bank of Augusta v. Earle*, 13 Peters, 519, by Taney, C. J., been the recognized rule of American law, that a corporation can have no legal existence out of the boundaries of the sovereignty by which it is created; that it exists by force of law, and where that ceases to operate, the corporation can have no existence; that it must dwell in the place of its creation, and cannot migrate to another sovereignty, and that it cannot hold meetings, pass votes, or do any corporate acts strictly so called outside of that sovereignty." *Smith v. Silver Valley Mining Co.*, 64 Md. 85 (1885). To the same point see *Morawetz on Corp.* (2d edition), § 488;

Taylor on Corp., § 382; *Wood on Railways*, § 139, p. 344.

² *Freeman v. Machias Water Power, &c., Co.*, 38 Me. 343 (1854); *Camp v. Byrne*, 41 Me. 525 (1867). But see *Heath v. Silverthorn Lead Mining, &c., Co.*, 39 Wis. 146 (1875), holding that the corporation may be estopped to deny the validity of acts done outside the State when the rights of third parties intervene.

³ *Bank of Augusta v. Earle*, 13 Peters, 519, 588; *Runyon v. Oester*, 14 Id. 122, 129; *Kerchner v. Gettys*, 18 S. C. 521; *Ex parte Schollenberger*, 96 U. S. 369 (1877); *Railroad Co. v. Harris*, 12 Wall. 65 (1870); *Bard v. Poole*, 12 N. Y. 495 (1855); *Mumford v. American Life Ins. Co.*, 4 Id. 463 (1851); *Stoney v. American Life Ins. Co.*, 11 Paige, 635 (1845); *New York Floating Derrick Co. v. New Jersey Oil Co.*, 3 Duer, 648 (1854).

⁴ *Ohio, &c., R. R. Co. v. McPherson*, 35 Mo. 13 (1864); *Bellows v. Todd*, 39 Iowa, 209, 217 (1874); *Armes v. Conant*, 36 Vt. 744 (1864); *Wood Hydraulic Hose Mining Co. v. King*, 45 Ga. 34 (1872); *McCall v. Byram Mfg. Co.*, 6 Conn. 428; *Wright v. Bundy*, 11 Ind. 398, 404; *Bassett v. Monte Cristo Mining Co.*, 15 Nev. 293; *Smith v. Alford*, 63 Barb. 415 (1866); *Galveston Railroad v. Cowdery*, 11 Wall. 459, 476 (1870). In *Copp v. Lamb*, 12 Me. 312 (1835), a meeting of the stockholders of a Maine

the particular office or place for meeting within the State, is specified in the charter or by-laws of the corporation. In that event a meeting held at a different place will be irregular, and the proceedings at such a meeting void and ineffectual.¹

§ 592. *Validity of corporate acts at meetings outside the State.*—There is a difference of opinion as to the effect of business transacted at a corporate meeting held beyond the borders of the State creating the corporation. Upon the one hand it is held that all the acts and proceedings of such a meeting are wholly invalid and void; that the corporation is not bound thereby, and that the meeting is as though it had never been.² But it is perhaps the sounder view to regard the votes and proceedings at such a meeting as voidable rather than void, and as capable of subsequent ratification by the corporation at a regular meeting.³ The corporation itself cannot allege that such proceedings are void. It is estopped from so doing.⁴ So also is any

corporation, in the State of New Hampshire, where they all resided, was held not illegal or void, but the circumstances of this case were peculiar. When a corporation migrates from the State of its creation into another State, ceasing entirely to do business in the former State and transacting all its business in the State to which it migrates, it loses its corporate rights and privileges, and the members become partners. *Merrick v. Brainard*, 38 Barb. 574 (1860). But see *Merrick v. Van Santvoord*, 34 N. Y. 208 (1866). See §§ 237-239.

¹ Where the customary place of meeting of a corporation is abandoned and a new place fixed upon in a regular and lawful manner, a meeting at the old place is irregular, and the proceedings at such a meeting are invalid. *Miller v. English*, 21 N. J. Law, 317 (1848). The meeting must be held at the usual place. *American Primitive Society v. Pilling*, 24 N. J. Law, 653 (1855). *Cf. McDaniels v. Flower Brook Mfg. Co.*, 22 Vt. 274 (1850).

² *Aspinwall v. Ohio, &c., R. R. Co.*, 20 Ind. 492, 497 (1863); *Wood v. Hydraulic Hose Mining Co.*, 45 Ga. 35 (1872); *Miller v. Ewer*, 27 Me. 509 (1847); *Freeman v. Machias Water Power, &c., Co.*, 38 Id. 343 (1854); *Hilles v. Parrish*, 14 N. J. Eq. 380 (1862); *Ormsby v. Vermont Copper Mining Co.*, 56 N. Y. 623 (1874); *Merrick v. Brainard*, 38 Barb.

574 (1860); see s. c. *sub nom. Merrick v. Van Santvoord*, 34 N. Y. 208 (1866).

³ *Ohio, &c., R. R. Co. v. McPherson*, 35 Mo. 13 (1864); *Freeman v. Machias Water Power, &c., Co.*, 38 Me. 343 (1854). The legislature may also validate the acts passed at such a meeting, in case it could have authorized the meeting in the first instance. *Graham v. Boston, Hartford & Erie R. R. Co.*, 118 U. S. 161, 178 (1886); affirming s. c. 14 Fed. Rep. 753 (1883). *Cf. Grenada Co. v. Brogden*, 112 U. S. 261 (1884); *Anderson v. Santa Anna*, 116 Id. 356 (1885); *Shaw v. Norfolk R. R. Co.*, 5 Gray, 162; *Howe v. Freeman*, 14 Id. 566.

⁴ *Heath v. Silverthorn Lead Mining, &c., Co.*, 39 Wis. 146 (1875). In this case the court says: "The question is, can the corporation repudiate its contracts on the ground that its officers, who executed them on its behalf, were chosen at a meeting held beyond the limits of this State? If this were a case of first impression, we should say upon principle, the company was estopped from availing itself of any such defense to defeat a recovery on its contracts; but the cases cited in the brief of counsel for the plaintiff, show that such a view is amply sustained by authority. These cases will not be particularly referred to in this opinion, but they will be found fully to sustain the proposition, that where a company has as-

stockholder who takes part in such a meeting.¹ If the corporation has been incorporated in two or more States, it is lawful to hold meetings of the stockholders in either State.² And proceedings at a meeting in any one of the States are valid in respect to the property of the corporation in all of them, without the necessity of the repetition of the meeting in any other of those States.³

§ 593. *By whom meetings are to be called.*—Where the time and place of a meeting, and the business to be transacted at that meeting, are not all fixed by charter or otherwise, so that the

sumed to exercise the franchises conferred by its charter, as this has done, it becomes a corporate body *de facto*, and the acts of its officers are binding upon the corporation. The company ought not to be permitted to say, in defense of an action upon its contracts entered into under such circumstances, that it had no legal existence when the contracts were executed, or that its officers were not duly elected or appointed. We have commented upon the fact that the charter created a private corporation, so far as it was possible for the legislature to bring one *in esse*, and constituted the incorporators a board of directors without further action. Our conclusion upon this point, therefore, is, that though the first meeting of the stockholders to elect directors was held in Chicago, this fact does not render the note and mortgage void as against the corporation."

¹ *Camp v. Byrne*, 41 Mo. 525 (1867); *Ohio, &c., R. R. Co. v. McPherson*, 35 Mo. 13 (1864). But mere neglect on the part of a shareholder who did not attend a meeting of this kind, or a mere failure to take affirmative action, for a period of time short of that prescribed by the Statute of Limitations, will not deprive that shareholder of his right to attack the proceedings as irregular and in fraud of his rights. *Ormsby v. Vermont Copper Mining Co.*, 56 N. Y. 623 (1874).

² *Graham v. Boston, Hartford & Erie R. R. Co.*, 118 U. S. 161 (1886); *Covington, &c., Bridge Co. v. Mayer*, 31 Ohio St. 317 (1877). *Cf. Richardson v. Vermont, &c., R. R. Co.*, 44 Vt. 613 (1872); *Culbertson v. Wabash Navigation Co.*, 4 McLean, 544 (1849). *Contra, Aspinwall v. Ohio, &c., R. R. Co.*, 20 Ind. 492 (1863).

³ *Graham v. Boston, Hartford & Erie R. R. Co.*, *supra*. In the opinion in this case, Blatchford, J., aptly says: "That a meeting in one of several States, of the stockholders of a corporation, chartered by all those States, is valid in respect to the property of the corporation in all of them, without the necessity of a repetition of the meeting in any other of those States, is, we think, a sound proposition. Whether it be or be not true, that proceedings of persons professing to act as corporators, when assembling without the bounds of the sovereignty granting the charter, are void, there is no principle which requires that the corporators of this consolidated corporation should meet in more than one of the States in which it has a domicile, in order to the validity of a corporate act. . . . The Boston, Hartford & Erie Co., therefore, though made up of distinct corporations chartered by the legislatures of different States, had a capital stock which was a unit, and only one set of shareholders who had an interest, by virtue of their ownership of shares of such stock, in all of its property everywhere. In its organization and action, and the practical management of its property, it was one corporation, having one board of directors, though, in its relations to any State, it was a separate corporation, governed by the laws of that State as to its property therein. It, therefore, had a domicile in each State, and the corporators or shareholders could, in the absence of any statutory provision to the contrary, hold meetings and transact corporate business in any one State, so as to bind the corporation in respect to its property everywhere."

stockholders are all bound to take notice of them, it is necessary that the meeting be called, and this call must be made by the properly authorized corporate authority.¹ In the absence of any special authority to any particular person to call meetings, the general agent of the corporation may make the call.² Statutory provisions as to who shall call the meetings are generally held to be merely directory. Accordingly, although the statute prescribes who shall call the meeting, yet other corporate officers than those prescribed in the statute may issue a valid call.³ Such also is the rule where the provision as to who shall call the meeting is made by by-law.⁴ The officers or agents of a corporation whose duty it is to call meetings, may, in case they neglect or refuse to issue the call, be compelled by *mandamus* to call a meeting at the instance of a shareholder who is injured by reason of their failure.⁵ Where there is no officer competent to call a meeting, it

¹ *Evans v. Osgood*, 18 Me. 213 (1841); *Congregational Society of Bethany v. Sperry*, 10 Conn. 200 (1834); *State of Nevada v. Pettineli*, 10 Nev. 141; *Angell & Ames on Corp.*, § 491. The notice itself should show that it is issued by an officer having authority to make a call. *Johnston v. Jones*, 23 N. J. Eq. 216 (1872); *Stevens v. Eden Meeting House Society*, 12 Vt. 688 (1839).

² *Stebbins v. Merritt*, 10 Cush. 27 (1852).

³ *Judah v. American Live Stock Insurance Co.*, 4 Ind. 333 (1853); *Chamberlain v. Painesville, &c. R. R. Co.*, 15 Ohio St. 225 (1864); *Newcomb v. Reed*, 12 Allen, 362 (1866). "The statute provides that as soon as ten per centum of the capital stock shall be subscribed, the persons named in the certificate of incorporation, or any three of them, may give notice for the stockholders to meet for the purpose of choosing directors. But we do not think it indispensable to an election, that the notice for it should be given by the persons named. Suppose they should all die before the time arrived for giving the notice, or, any of the many other contingencies should occur which would prevent their action, could not an election be had? If the necessary amount of stock has been obtained, and at a meeting of the stockholders for the purpose they elect directors, the validity of their acts cannot be questioned collaterally on account of the irregularity

in their election. The statute in regard to the notice is directory." *Chamberlain v. Painesville, &c. R. R. Co.*, *supra*, p. 250. Where three persons are appointed to make a call, and one of them calls the meeting of incorporation, the other two making no objection, the organization of the company at the meeting so called is valid. *Walworth v. Brackett*, 98 Mass. 98 (1867).

⁴ *Chamberlain v. Painesville, &c. R. R. Co.*, 15 Ohio St. 225 (1864). Where a by-law provides that special meetings may be called by the president, or in his absence by the secretary, on application made by ten members in writing, the directors may call a special meeting without such an application. *Citizens' Mutual Fire Ins. Co. v. Sortwell*, 8 Allen, 217 (1864). But where a by-law authorizes the trustees to call a meeting, a meeting called by the president is irregular. *State of Nevada v. Pettineli*, 10 Nev. 141 (1875). When the by-laws require a call in writing, a call by parol is insufficient. *Stevens v. Eden Meeting House Society*, 12 Vt. 688 (1839).

⁵ *State of Nevada v. Wright*, 10 Nev. 167 (1875); *People v. Board of Governors of Albany Hospital*, 61 Barb. 397 (1871); *McNeely v. Woodruff*, 13 N. J. Law, 352 (1833). In this case the court say: "It is made the duty of the directors to notify an election within thirty days. What is the consequence if they neglect this duty? The penalty is not

has been held that the corporation cannot carry on business until properly reorganized under a new charter.¹ But it is doubtful whether such a rule would be held good at the present day. If, upon the organization of a corporation, a majority of the subscribers refuse to proceed in calling a meeting, the minority may call it, and bind the corporation.²

§ 594. *When the stockholders are entitled to notice of corporate meetings.*—If the time and place at which a corporate meeting is to be held is distinctly fixed in the charter, or by a by-law, or by usage, this is of itself sufficient notice to all the stockholders, and no further call or notice of that meeting is necessary.³ But a by-law which fixes the day of meeting without also fixing the hour, is insufficient as a notice to stockholders of that meeting.⁴ It is a general and settled rule of law that notice, in some way or other, must be given to every person entitled to be present at a corporate meeting.⁵ When, therefore, no sufficient notice is given by charter, or statute, or by-law, each stockholder

to be a forfeiture of the franchise; there is not such a word in the latter statute. Such a forfeiture cannot arise by implication, for forfeitures are odious except when inflicted by positive enactment. The consequence of neglecting their duty is simply this: that after thirty days the stockholders may compel them to do their duty by *mandamus* or otherwise immediately. It was not intended to impair the charter right of holding an election at any time, but to hasten and quicken the directors in using it, and putting it in the power of the stockholders to compel them to do it, if they should neglect for thirty days." *Cf. Regina v. Aldham, &c. Insurance Society*, 6 Eng. L. & Eq. 365 (1851).

¹ *Goulding v. Clark*, 34 N. H. 148 (1856).

² *Busey v. Hooper*, 35 Md. 15 (1871).

³ *Warner v. Mower*, 11 Vt. 385, 393 (1839); *State v. Bonnell*, 35 Ohio St. 10, 15 (1878). *Cf. Atlantic Mutual Fire Ins. Co. v. Sanders*, 36 N. H. 252 (1858); *Sampson v. Bowdoinham Steam Mill Co.*, 36 Me. 78 (1854); *Moore v. Hammond*, 6 Barn. & C. 456 (1827). Where a special day has been fixed for the election of a city official, it is not competent for a board of aldermen, at an intervening meeting, to rescind the resolution, and

go at once into an election. *People v. Batchelor*, 22 N. Y. 128 (1860).

⁴ The fact that one of the by-laws of the corporation fixes the day upon which the annual meeting of the corporation shall be held, is not of itself a sufficient notice of the time and place at which the meeting is to be held. There must be an express notice of the day, hour, and place of meeting. Otherwise, unless all the stockholders are present and consent, either in person or by proxy, the meeting cannot legally be held. *San Buenaventura Commercial, &c. Co. v. Vassault*, 50 Cal. 534 (1875). Though the by-laws of a corporation fix the date of the annual meeting, that of itself will not be notice of the meeting. Notice must be given of the place of the meeting, and a provision of the charter for the calling of all meetings is a mandatory provision, applicable alike to general and special meetings. *United States v. McKelder*, 8 Rep. 778 (Sup. Ct. Dist. of Col., 1879).

⁵ "To support the validity of corporate acts, each member must be actually summoned." *Angell & Ames on Corp.*, § 492. "Due notice of the time and place of a corporate meeting is, by the English law, essential to its validity, or its power to do any act which shall bind the corporation." *Dillon on Munic. Corp.*, § 200.

is entitled to an express, personal notice of every corporate meeting.¹ No usage can operate to excuse a failure to give such a notice,² and it has even been held that custom or by-laws cannot change or abrogate the right to a notice of corporate meetings.³

§ 595. *The essential elements of a notice of a meeting are time, place, and business.*—The contents of the notice depends upon the character of the meeting. There are three matters concerning every corporate meeting of which the members are entitled to notice, namely, the time, the place, and the business proposed to be transacted. Some or all of these may be known to him, by virtue of a charter provision, or a by-law, or a statute. But if any one of them is not known in that way, the stockholders are entitled to an actual notice thereof. Accordingly, it is the rule that, in the absence of other valid notice, the call must specify the time and place of meeting, and the business to be considered.⁴ The precise hour at which the meeting is to be held must be stated in the notice.⁵

¹ *Wiggin v. Freewill Baptist Church*, 8 Metc. 301 (1844); *People v. Albany, &c. R. R. Co.*, 55 Barb. 344 (1869); *Commonwealth v. Cullen*, 13 Penn. St. 133 (1850); *Jackson v. Hampden*, 20 Me. 37 (1841); *McDaniels v. Flower Brook Manfg. Co.*, 22 Vt. 274 (1850); *San Buenaventura Commercial, &c. Co. v. Vassault*, 50 Cal. 534 (1875); *Stockholders of the Shelby R. R. Co. v. Louisville, &c. R. R. Co.*, 12 Bush. 62 (1876); *Rex v. Langhorn*, 4 Ad. & El. 538 (1836); s. c. 6 Nev. & M. 203; 2 Id. 618; *Moore v. Hammond*, 6 Barn. & C., 456 (1827); *Smyth v. Darley*, 2 H. of L. Cas. 789 (1849). *Cf.* *Stebbins v. Merritt*, 10 Cush. 27 (1852); *People v. Batchelor*, 22 N. Y. 128, 134 (1860); *Shortz v. Unangst*, 3 Watts & S. 45 (1841); *Cannon v. Trask*, L. R. 20 Eq. 669 (1875); *MacDougall v. Gardiner*, L. R. 1 Chan. Div. 13 (1875); *People v. Peck*, 11 Wend. 604 (1834).

² *Wiggin v. Freewill Baptist Church*, 8 Metc. 301 (1844).

³ *The King v. Attwood*, 4 B. & Ad. 481 (1833); *The King v. Westwood*, 7 Bing. 1 (1830); *The King v. Bird*, 13 East, 367 (1811); *Green v. Mayor of Durham*, 1 Burr. 127 (1757).

⁴ *The King v. Hill*, 4 Barn. & C., 426 (1825). *In re Bridport Old Brewery Co.* L. R. 2 Chan. 191 (1866); *In re Silkstone*

Fall Colliery Co., L. R. 1 Chan. Div. 38 (1875). *Cf.* *Wills v. Murray*, 4 Exch. 843 (1850).

⁵ *San Buenaventura Commercial, &c. Co. v. Vassault*, 50 Cal. 534 (1875). Here the court said: "Conceding that this by-law is notice *per se*, that the annual meeting of the stockholders will be held on the third Monday in April of each year, it is insufficient as a notice of the point of time during that day at which the meeting is to be held. . . . The fact that the by-law here names a day upon which, instead of a week within which, the annual meeting is to be held, while it may diminish, does not remove the uncertainty as to the time at which it is to be held. A meeting held on that day, at any time within the business hours customarily observed in San Francisco, might be fairly claimed to have been held pursuant to the notice. A body of the stockholders might meet at ten o'clock a. m. of that day and proceed to transact the business of the annual meeting, including the election of trustees; at a later hour of the same day, say at twelve o'clock m., another body of the stockholders, it may be, representing the actual majority of the stock, might convene and proceed to elect a different board of trustees, and each of these bodies might equally claim to have proceeded pursu-

In general the notice need not specify the business to be considered where the meeting is one prescribed by charter, or where the business is prescribed by charter, or statute, or by-law, and no unusual business is to be transacted.¹ But if the meeting is to be held at a time not provided by the charter, or if unusual business is to be transacted at a meeting which is a customary one, the call must specify particularly such unusual business.² Thus at a meeting called to alter the by-laws and transact other business an election cannot lawfully be held.³ Nor can an assessment be levied at a special meeting when the stockholders were not duly notified that that matter would come up for consideration.⁴ At a special meeting which has been called for a particular purpose only the business specified in the call can lawfully be transacted.⁵ The transaction, however, of business other than that for which

ant to the notice contained in the by-law of the corporation. In view of the frequent and constantly recurring struggles by different combinations of stockholders to obtain control of the corporate direction, often resulting in serious embarrassment to the corporate interests, it is highly important that the notice should be so definite and certain in its character as to leave no room for controversies such as the one now before us."

¹ *Sampson v. Bowdoinham Steam Mill Co.*, 36 Me. 78 (1854); *Warner v. Mower*, 11 Vt. 385 (1839); *People's Insurance Co. v. Westcott*, 14 Gray, 440 (1860). See also *Wills v. Murray*, 4 Exch. 843 (1850); s. c. 19 L. J. Exch. 209; *South School District v. Blakeslee*, 13 Conn. 227 (1839); *Merritt v. Farris*, 22 Ill. 303 (1859); *People v. Batchelor*, 22 N. Y. 128 (1860).

² *In re Bridport Old Brewery Co.*, L. R. 2 Chan. 191 (1866); *In re Silkstone Fall Colliery Co.*, L. R. 1 Chan. Div. 38 (1875); *Atlantic De Laine Co. v. Mason*, 5 R. I. 463 (1858); *Tuttle v. Michigan Air Line R. R. Co.*, 35 Mich. 247 (1877); *Shelby R. R. Co. v. Louisville, &c. R. R. Co.*, 12 Bush, 62 (1876); *Merritt v. Farris*, 22 Ill. 303 (1859). *Cf.* *Ashbury Ry., Carriage & Iron Co. v. Riche*, L. R. 7 H. of L. 653 (1875); *Zabriskie v. Cleveland, &c. R. R. Co.*, 23 How. 381 (1859); *Savings Bank v. Davis*, 8 Conn. 192 (1830). "The decision of this case then turns on the question whether the extraordinary resolution of the 2d of October, 1866, was valid or not. The first part of this resolution is, that it had been proved to the satisfaction of the company, that

the company could not, by reason of its liabilities, continue its business. But the notice did not state that an extraordinary resolution to wind up the company would be proposed; nor did it give any intimation that it was proposed to consider at the meeting the question whether the company was able to continue its business. Now it is evidently of great importance to shareholders that they should have proper notice what subjects are proposed to be considered at a meeting, and I do not think that in the present case they had such notice. I do not say that it was necessary to follow in the notice the precise terms of the company's act (sect. 129, clause 2), but it appears to me that the shareholders were entitled to have a notice which would give them to understand that it was proposed to pass an extraordinary resolution to wind up the company. It is of great importance that the steps taken in a matter of such consequence as the resolving to wind up a company should be perfectly regular, and in the present case I think that there was no sufficient notice." *In re Bridport Old Brewery*, L. R. 2 Chan. 191, 194 (1866).

³ *People's Insurance Co. v. Westcott*, 14 Gray, 440 (1860). *Cf.* *Rex v. Town of Liverpool*, 2 Burr. 723 (1759); *Rex v. Doncaster*, Id. 738.

⁴ *Atlantic De Laine Co. v. Mason*, 5 R. I. 463 (1858). See also *Smith v. Erb*, 4 Gill (Md.), 437.

⁵ *Warner v. Mower*, 11 Vt. 385 (1839). *Cf.* *Ex parte Fox*, L. R. 6 Chan. 176 (1871).

the meeting was called will not invalidate the entire proceedings at that meeting. There is only an invalidity *pro tanto*.¹

§ 596. *Service of the notice*.—If the particular form of the notice, or the manner in which it shall be served, is prescribed by charter or by law or by statute, the notice must be given in that manner, otherwise all the proceedings of the meeting are invalid.² In the absence of an express provision as to the manner of making a call, it is the common-law rule that each member of the corporation is entitled to a personal service of the notice.³ But a written or verbal notice left at a place of business, in charge of a member of the stockholder's family, has been held sufficient.⁴ The physical or mental incapacity of one of the stockholders will not excuse a failure to give him notice of a meeting, and it is very clear that the meeting may lawfully convene and transact business although one of the members is incapable, by reason of imbecility, of receiving the notice.⁵ But the absence of a stockholder from home does not excuse a failure to leave the notice.⁶ And where one

¹ *In re* British Sugar Refining Co., 3 Kay & J. 408, 413 (1857); *Graham v. Van Dieman's Land Co.*, 1 Hurl. & N. 541 (1856); *Cleve v. Financial Corporation*, L. R. 16 Eq. 363 (1873). *Cf. In re* Irrigation Co. of France, L. R. 6 Chan. 176 (1871). But it is held that at a special meeting, all the members being present and consenting, business other than that specified in the call may lawfully be transacted. *The King v. Theodorick*, 8 East, 543 (1807); *In re* The Joint Stock Co.'s Act 1856, 3 Kay & J. 408 (1857); *San Buenaventura Commercial Mining, &c. Co. v. Vassault*, 50 Cal. 534 (1875). But see *People's Mutual Ins. Co. v. Westcott*, 14 Gray, 440 (1860). All acts done by a portion of the stockholders at a meeting so-called or convened as to have the appearance of trickery, secrecy, or fraud, are invalid; and surprise and fraud in respect to any part of the stockholders with regard to the meeting will invalidate all proceedings at that meeting. *People v. Albany, &c. R. R. Co.*, 55 Barb. 344 (1869); *MacDougall v. Gardiner*, L. R. 1 Chan. Div. 13 (1875).

² *Stockholders of Shelby R. R. Co. v. Louisville, &c., R. R. Co.*, 12 Bush, 62 (1876); *Warner v. Mower*, 11 Vt. 385 (1839); *Reilly v. Oglebay*, 25 West. Va. 36 (1884); *Johnston v. Jones*, 23 N. J. Eq. 216 (1872); *Stevens v. Eden Meeting*

House Society, 12 Vt. 688 (1839); *Swansea Dock Co. v. Levien*, 20 L. J. Exch. 447 (1851). *Cf. Citizens Mutual, &c. Co. v. Sortwell*, 8 Allen, 217 (1864); *Smith v. Law*, 21 N. Y. 296 (1860). The manner of making the call may be prescribed by by-law, and when so prescribed, provided the by-law is reasonable, calls made in that way are valid. *Taylor v. Griswold*, 14 N. J. Law, 222 (1834).

³ *Tuttle v. Michigan Air Line R. R. Co.*, 35 Mich. 247 (1877); *Stevens v. Eden Meeting House Society*, 12 Vt. 688 (1839); *Wiggin v. Freewill Baptist Church*, 8 Metc. 301 (1844); *Stow v. Wyse*, 7 Conn. 214 (1828); s. c. 18 Am. Dec. 99; *Savings Bank v. Davis*, 8 Conn. 191 (1830); *Taylor v. Griswold*, 14 N. J. Law, 222 (1834); *Harding v. Vandewater*, 40 Cal. 77. *Cf. Porter v. Robinson*, 30 Hun, 209 (1883); *Rex v. Doncaster*, 2 Burr. 738; *Rex v. Town of Liverpool*, Id. 723 (1759).

⁴ *Williams v. German Mutual Fire Ins. Co.*, 68 Ill. 387 (1873). See, however, *Stevens v. Eden Meeting House Society*, 12 Vt. 688 (1839).

⁵ *Stebbins v. Merritt*, 10 Cush. 27 (1852).

⁶ *Jackson v. Hampden*, 20 Me. 37 (1841). In *Porter v. Robinson*, 30 Hun, 209 (1883), it is held that notice need not be given to a member of a board of school trustees, the board being a body

of the stockholders dies after notice of a meeting, but before the meeting convenes, and no administrator is appointed in time to act at that meeting, there is on this account no ground to impeach the regularity of the meeting.¹ A pledgee of shares is not entitled to a notice of corporate meetings² since the pledgor is entitled to vote upon the stock until the contract of bailment is broken and foreclosed.³

§ 597. *Notice must be served a reasonable time before the meeting.*—The notice must be served upon the stockholders a reasonable or customary time before the day of the meeting,⁴ where by statute it is provided that thirty days notice shall be given of certain corporate meetings, that length of time suffices for notice of other meetings of the same corporation.⁵

§ 598. *The division of meetings into ordinary and extraordinary.*—Corporate meetings of stockholders are frequently divided, both by the judges and the text-writers, into two classes, the first being special or extraordinary, and the second being ordinary, regular, stated, or general. By reason of this attempt at classification much confusion has been introduced into the law without any corresponding advantage. The terms employed to distinguish the various kinds of meetings are used in different senses by different writers, so that it is difficult to define them in

corporate, who is absent from the State and cannot attend the meeting, and that a failure to notify such a member will not render the proceedings at the meeting irregular or invalid. The court said: "The object of notice is to give the person notified an opportunity to attend. There is no other virtue in the notice. Now when a person elected as trustee is at the time of his election in a distant State, and continues there all the time until after the meeting in question, never having had any formal notice of his election, it would be unreasonable to say that a meeting was made invalid by a failure to give him notice thereof. Must a personal notice be served on him in Minnesota? Or, if a notice left at his house is sufficient, of what use would it be to one who was beyond its reach? It cannot be necessary to do an act which, when done, would be of no use. By remaining where he could not attend the meetings of the board of education, S. practically waived

any notice of such meeting, and indeed put it beyond the power of the proper officer to give any." Subsequently the member returned and acted as trustee. Members of English joint-stock companies residing abroad are not entitled to any notice of corporate meetings. *Ex parte Union Hill Company*, 22 L. T. 400.

¹ *Freeman's National Bank v. Smith*, 13 Blatchf. 220 (1875).

² *McDaniels v. Flower Brook Manfg. Co.*, 22 Vt. 274 (1850).

³ *New York, &c. R. R. Co. v. Schuyler*, 38 Barb. 534, 542 (1860), per Ingraham, J., *arguendo*, *vide*, § 468.

⁴ In the *Matter of the Long Island R. Co.*, 19 Wend. 37 (1837); *Wiggin v. Freewill Baptist Church*, 8 Metc. 301 (1844). *Cf. Covert v. Rogers*, 38 Mich. 368, where a similar rule is declared as to notice to directors of their meetings.

⁵ *Shelby R. R. Co. v. Louisville, &c. R. R. Co.*, 12 Bush, 62 (1876).

such a way as to avoid confusion. It seems, however, to be a very generally accepted principle that if the time, or the place, or the business of a meeting is unusual, that meeting is special or extraordinary, at least to the extent that any one or more of these three matters are unusual. Accordingly, when neither the time, nor place, nor business of a meeting is unusual, that meeting is a general, ordinary, or regular meeting.¹

¹ *Mason v. Atlantic De Laine Co.*, 5 R. I. 463 (1858); *Zabriskie v. Cleveland, &c. R. R. Co.* 23 How. 381 (1859); *People's Insurance Co. v. Westcott*, 14 Gray, 440 (1860); *Sampson v. Bowdoinham Steam Mill Co.*, 36 Me. 78 (1854). In *Warner v. Mower*, 11 Vt. 385, 391 (1839). Redfield, J., in an exceedingly luminous opinion, insists that this distinction between an ordinary and an extraordinary meeting is a most material one. At a regular annual meeting, that is where the meeting is stated and general, any and all proper corporate business may be transacted. *Warner v. Mower*, 11 Vt. 385, 392 (1839). At the annual meeting any business may be transacted, provided it be within the scope of the corporate enterprise. *Schoff v. Bloomfield*, 8 Vt. 472 (1836). A meeting of stockholders, under § 5122 of the Revised Statutes of the United States, for the purpose of making petition that the company be declared a bankrupt, is not such a meeting as is provided for by the New York Statute of 1848 (Laws of 1848, chap. 40, § 21) and hence it is not necessary that it be called in the manner prescribed in that section. *Freeman's National Bank v. Smith*, 13 Blatchf. 220 (1875). A stated meeting is usually a general meeting. *Warner v. Mower*, *supra*. Every member is entitled to personal notice of a special meeting. *Warner v. Mower*, *supra*. Cf. *Kynaston v. Mayor of Shrewsbury*, 2 Strange, 1051 (1837); *Rex v. Town of Liverpool*, 2 Burr. 723, 728 (1759); *Rex v. Mayor and Aldermen of Carlisle*, 1 Strange, 385 (1720); *Stow v. Wyse*, 7 Conn. 214 (1828); s. c. 18 Am. Dec. 99 and the note. In England a general meeting of every company formed under the Companies Acts (25 & 26 Vict. c. 89; 30 & 31 Vict. c. 131; 40 & 41 Vict. c. 26; 42 & 43 Vict. c. 76; 43 Vict. c. 19), must be held once at least in every year. In default of any regulations in the articles as to the summoning of general meetings, seven days

notice in writing sent to the shareholders is sufficient. With respect to the manner of the notice it is enacted, as regards cost book mining companies, that "a notice to be served by a company for any purpose of this act on a shareholder shall be served personally, or shall be served by prepaid letter sent by post addressed to him at his address as entered in the cost book, in which case the notice shall be taken as served at the time when the letter containing it was put into the post office; and in proving such notice it shall be sufficient to prove that the letter was properly addressed and prepaid and was put into the office, and the time when it was put in. As regards a company existing at the passing of this act, the address of a shareholder as known to the purser at the passing of this act shall be and remain entered in the cost book as his address, unless and until he gives notice in writing to the contrary" (32 & 33 Vict. chap. 19, § 8); and this is substantially the rule which applies to notices to members of other companies. Art. 95 & 97 of Table A, to the Companies Act of 1862. See, for a construction of these articles, *In re London, &c. Fire Insurance Co.*, L. R. 24 Chan. Div. 149. The Companies Act of 1862 recognizes only one description of general meeting. But by Table A of that act there is a distinction drawn between ordinary general meetings and extraordinary general meetings. Table A, art. 31. Ordinary meetings or ordinary general meetings are those convened at regular intervals, not exceeding one year, in accordance with the articles. All other meetings of the company are extraordinary meetings. The first general meeting of the company must be held within four months of the registration of the company, and may be either an ordinary or extraordinary meeting. Subject to the articles of association, any business of which proper notice has been given may be transacted at any meeting.

§ 599. *Waiver of notice.*—The stockholder may, in general, waive his right to have a notice of a corporate meeting duly served upon him.¹ But where the giving of the notice is prescribed by statute, it is held that the notice cannot be waived.² This is not, however, a universal rule.³ The presence and consent of all who have a right to the notice is a waiver of it.⁴ So participation as an officer in issuing the call is a waiver by him of informalities as to that call,⁵ and recognition of an agent appointed at a certain meeting, by dealing and offering to deal with him as the agent of the company, is a waiver of the right to notice of that meeting.⁶ One stockholder cannot avail himself of the neglect of the corporate officers to give due notice to another stockholder who does not himself complain.⁷ But the waiver of all the stockholders is essential in order to validate the

Extraordinary meetings may be convened at any time, subject to proper notice, at the option of the directors, or on a requisition in writing signed by a specified number of shareholders. The Companies Act of 1862, 25 & 26 Vict. chap. 89, §§ 49, 50, 51, 52; Shelford on Joint Stock Companies, 74, 204; Hurrell & Hyde on Joint Stock Companies, 56.

¹ *Turquand v. Marshall*, L. R. 4 Chan. 376 (1869); *Smallcombe v. Evans*, L. R. 3 H. of L. 249 (1868); *Phosphate of Lime Co. v. Green*, L. R. 7 C. P. 43 (1871); *Richardson v. Vermont, &c.*, R. R. Co., 44 Vt. 613 (1872); *Judah v. American, &c., Ins. Co.*, 4 Ind. 333 (1853); *Jones v. Milton, &c., Turnpike Co.*, 7 Id. 547 (1856).

² *United States v. McKelden*, 8 Rep. 778 (1879); *In the Matter of the Long Island R. R. Co.*, 19 Wend. 37 (1837). See *The King v. Theodorick*, 8 East, 543 (1807); *People v. Peck*, 11 Wend. 604 (1834).

³ *Kenton Furnace R. R. & Manfg. Co. v. McAlpin*, 5 Fed. Rep. 737 (1880).

⁴ *Stebbins v. Merritt*, 10 Cush. 27 (1852); *People v. Peck*, 11 Wend. 604 (1834); *Kenton Furnace R. R. & Manfg. Co. v. McAlpin*, 5 Fed. Rep. 737 (1880); *Ex parte Faris*, 26 L. J. Chan. 369 (1856); *The King v. Chetwynd*, 7 Barn. & C. 695 (1828). Cf. *San Buenaventura Commercial, &c., Co. v. Vassault*, 50 Cal. 534 (1875); *In re British Sugar Refining Co.*, 3 Kay & J. 408 (1857); and see *State of Nevada v. Pettineli*, 10 Nev. 141 (1875). In *Jones v. Milton, &c., Turnpike Co.*, 7

Ind. 547 (1856), the court said: "It is objected that notice of the meeting for the election of directors was not proved, but the objection is, in this case, unimportant, as, from the evidence, it appears that the subscribers here sued were present by their proxy, and voted at the election." The stockholder who participates in the proceedings at a meeting is estopped to question the sufficiency of his notice. *In re The Joint Stock Co.'s Act*, 1856, 3 Kay & J. 408 (1857); *Williams v. Financial Corporation*, L. R. 16 Eq. 363, 375 (1873).

⁵ *Bucksport, &c., R. R. Co. v. Buck*, 68 Me. 81 (1878); *Schenectady, &c., Plankroad Co. v. Thatcher*, 11 N. Y. 102 (1854).

⁶ *Bryant v. Goodnow*, 5 Pick. 228 (1827).

⁷ *Schenectady, &c., Plankroad Co. v. Thatcher*, 11 N. Y. 102 (1854). In this case the court said: "The court rejected the offer of the defendant to prove that no notice had been given of the first election of directors. I think this was properly rejected, on the ground that the defendant could not avail himself of a neglect to give notice to any other stockholder. The defendant himself was present at that meeting and voted, and was elected a director. He has not suffered by an omission to serve notice, and he is not in a situation to object as to others." See also *In the Matter of the Election of Directors of the Mohawk & Hudson R. R. Co.*, 19 Wend. 135 (1835); and cf. *Samuel v. Holliday*, 1 Woolf. 400.

proceedings at a meeting not properly called.¹ Accordingly, where one shareholder is absent from a meeting assembled without a call, or refuses his assent, the proceedings are irregular and invalid.²

§ 600. *Notice is presumed to have been regularly given.*—It is a presumption of law that proper and valid notice of a corporate meeting has been duly given to every stockholder, and that the meeting itself was regularly and lawfully held. The burden of proof is, therefore, upon him who alleges want of notice or insufficiency of notice, or attacks the regularity and validity of the proceedings.³

§ 601. *Adjourned meetings.*—An adjourned meeting is but a continuation of the meeting which has been adjourned, and when that meeting was regularly called and convened, and duly adjourned, the shareholders may, at the adjourned meeting, consider and determine any corporate business that might lawfully have been transacted at the original meeting.⁴ Accordingly, where the charter or by-laws of a corporation prescribe that when less than a *quorum* are present at a regular meeting, duly called and convened, they may adjourn to a future day, if at the adjourned meeting a *quorum* is present that *quorum* is competent to exercise the ordinary corporate powers, and to transact whatever business might have been proposed and concluded at the regular meeting, although the absentees have no other notice of the meeting than that with which they are chargeable from the by-law, by virtue of which the regular meeting was adjourned.⁵ But where there is an absence of good faith, and an adjourned meeting is held in such a way as to prevent certain of

¹ State of Nevada v. Pettineli, 10 Nev. 141 (1875).

² Farwell v. Houghton Copper Works, 8 Fed. Rep. 66 (1881); Moore v. Hammond, 6 Barn. & C. 456 (1827); Rex v. Langhorn, 4 Ad. & El. 538 (1836); s. c., 2 Nev. & M. 618; 6 Id. 203; Smyth v. Darley, 2 H. of L. Cas. 789 (1849); Rex v. Theodorick, 8 East, 548 (1807); Rex v. Gaborian, 11 Id. 86, n. 87, n. Cf. People's Insurance Co. v. Westcott, 14 Gray, 440 (1860); Dillon on Munic. Corp., § 202; Angell & Ames on Corp., § 495.

³ McDaniels v. Flower Brook Manf. Co., 22 Vt. 274 (1850); Porter v. Robin-

son, 30 Hun, 209 (1883); Sargent v. Webster, 13 Metc. 497 (1847); Medical & Surgical Society v. Weatherly, 75 Ala. 248. Cf. Lane v. Brainerd, 30 Conn. 565 (1862); Pitts v. Temple, 2 Mass. 538 (1807); Copp v. Lamb, 12 Me. 312 (1835).

⁴ Granger v. Grubb, 7 Phila. 350 (1870); Farrar v. Perley, 7 Me. 404 (1831); Schoff v. Bloomfield, 8 Vt. 472 (1836); Warner v. Mower, 11 Id. 385 (1839). Cf. The Queen v. Grimshaw, 10 Q. B. 747 (1847); People v. Batchelor, 22 N. Y. 128 (1860).

⁵ Smith v. Law, 21 N. Y. 296 (1860).

the stockholders from knowing of it, the proceedings are invalid.¹ Where the original meeting was duly called and convened, the stockholders are not entitled to any other notice of the adjourned meeting than that which is implied in the adjournment.²

¹ *State v. Bonnell*, 35 Ohio St. 10 (1878).

² *United States v. McKelden*, 8 Rep. 778 (1879); *Smith v. Law*, 21 N. Y. 296 (1860); *People v. Batchelor*, 22 Id. 128 (1860); *Warner v. Mower*, 11 Vt. 385 (1839); *Schoff v. Bloomfield*, 8 Id. 472 (1836); *Farrar v. Perley*, 7 Me. 404 (1831); *The Queen v. Grimshaw*, 10 C. B. 747 (1847); *Wills v. Murray*, 4 Exch. 843 (1850); s. c., 19 L. J. Exch. 209; *Rex v. Carmarthen*, 1 Maul. & Sel. 702. In *Scadding v. Lorant*, 3 H. of L. Cas. 418 (1851), a most carefully considered case, which went from the Court of Queen's Bench, where it was commenced, through the Court of Exchequer Chamber to the House of Lords, in which it was conceded that the notice given of the original meeting was in all respects regular and suffi-

cient, although the notice actually given omitted to state the purpose for which the meeting was to be held, but the ground was taken that no sufficient notice had been given of the adjourned meeting, the court said: "We are unanimously of opinion that the vote was not rendered invalid by reason of the alleged defect in the notice of the adjourned meeting. It was sufficient to give notice on the church-door of the purpose for which the first meeting was to be held, and that notice having been duly given, we think that the notice so given extended to all the adjourned meetings—such adjourned meetings being held for the purpose of completing the unfinished business of the first meeting, and being in continuation of that meeting." See, however, *Gowen's Appeal*, 10 Week. Notes Cas. 85 (1881).

CHAPTER XXXVII.

CORPORATE MEETINGS.—ELECTIONS AND OTHER BUSINESS. .

A.—ELECTIONS.

- § 602. Scope of the subject.
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B.—OTHER CORPORATE FUNCTIONS BELONGING TO THE STOCKHOLDERS AS DISTINGUISHED FROM THE DUTIES OF DIRECTORS.

- 621. The general method of transacting business.
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A.—ELECTIONS.

§ 602. *Scope of the subject.*—The business which the stockholders of a corporation, in meeting assembled, have the power to transact, is not extensive, although generally of great importance. Generally the meeting elects the corporate officers, listens to reports of the condition of the corporation, and adjourns. Consequently the law relative to the business which a corporate meeting may transact is chiefly the law regulating corporate elections. It happens, however, occasionally, that important changes are to be made in the corporate enterprise. In that case, such changes are generally authorized by the corporate meetings. The preceding chapter explained the legal method of calling together a corporate meeting. This chapter treats of the business which may be transacted at such meetings, and also the methods of its transaction.

§ 603. *Elections are to be by the stockholders.*—At common law the directors of a corporation are to be elected by the stockholders, in corporate meeting assembled. Generally this is declared to be the law by charter or statutory provisions. The subordinate officers and agents of the corporation are generally elected or appointed, not by the stockholders, but by the directors. All these matters, however, are the usual subjects of statutory regulations.

§ 604. *Who shall preside at elections.*—In the absence of an express provision by statute, or in the charter, it is not essential to the validity of a corporate election that the corporate officers preside at the meeting at which the election is held.¹ Generally the charter or the statutes provide for inspectors to superintend corporate elections. In an emergency, however, in which the forms of procedure prescribed by the charter, in respect to elections, fail to accomplish the purposes contemplated, owing to the fact that the necessary inspectors do not act, it is competent for the corporators themselves to exercise the power of appointing inspectors, or to provide for their appointment for the purpose of an election.² So also where the regular inspectors are restrained by an order of court from acting, the stockholders may appoint other inspectors and proceed.³

§ 605. *Conducting, opening, and closing elections.*—The form or mode of conducting an election is, in general, not material, provided it violates no positive provision of the charter or of a statute regulating it; is orderly, and in good faith; and is conducted by authorized or proper persons.⁴ Where no time is specified by law within which the polls must be kept open, it rests within the sound discretion of the inspectors to say when

¹ *People v. Twaddell*, 18 Hun, 427 (1879). This was a case of an election of trustees of a religious corporation, and the court held that where such a corporation, duly organized and constituted, had for several years failed to elect trustees, there being no provision authorizing those formerly elected to hold over until their successors are chosen, or requiring the trustees or other officers to preside at or do any act in relation to the election, it is within the proper power of the corporators themselves, without any new

legislative aid, to meet voluntarily at the time designated in the constitution for an election, and proceed to the election of a new board of trustees.

² *Matter of Wheeler*, 2 Abb. Prac. (N. S.) 361 (1866). The failure of the inspectors so appointed to take the prescribed oath will not invalidate the election.

³ *People v. Albany, &c.*, R. R. Co., 55 Barb. 344 (1869).

⁴ *Fox v. Allensville, &c.*, Turnpike Co., 46 Ind. 31 (1874).

the polls shall close.¹ So also it is held, that holding the polls open after the hour specified in the notice for them to close, will not, where the inspectors exercise a reasonable discretion, invalidate an election.² And, as a general rule of law, where, in the election of corporate officers, no particular mode of proceeding is prescribed by law, if the wishes of the corporators have been fairly expressed, and the election was conducted in good faith, it will not be set aside on account of any informality in the manner of conducting it.³

§ 606. *Mandamus to compel election.*—At common law *mandamus* lies to compel an election of corporate officers.⁴ But in Louisiana, if the corporate officers die, resign, or refuse to act, and the stockholders neglect or refuse to appoint or elect others in their place, a court of equity will appoint a receiver or manager *ad interim*, for the purpose of winding up and putting an end to the concern.⁵

¹ In the Matter of the Chenango County Ins. Co., 19 Wend. 634 (1839).

² In the Matter, &c., of the Mohawk & Hudson R. R. Co., 19 Wend. 135 (1838), the court saying: "The trustees acted properly in taking the requisite time, notwithstanding they were called on to close the poll at one o'clock. I much doubt whether the time could, in virtue of a by-law, be tied up to a certain hour of the day; but in this case it was not attempted. I have no doubt that in case of actual necessity the business might have been extended even to the next day. Every principle of construction is in favor of full time, otherwise business may be badly done by being hurried, or embarrassed and defeated by the raising of dilatory objections and protracted examination and discussion. (Rex v. Mayor, &c., of Carmarthen, 1 Maule & Sel. 697.)" See *People v. Albany, &c.*, R. R. Co., 55 Barb. 344 (1869).

³ *Philips v. Wickham*, 1 Paige, 590 (1829).

⁴ *People v. Board of Overseers of Albany Hospital*, 61 Barb. 397 (1871); *State of Nevada v. Wright*, 10 Nev. 167 (1875); *People v. Cummings*, 72 N. Y. 433 (1878). In this case the court say: "If trustees could keep themselves in office by not having an annual election, the stockholders would be powerless, and they might perpetuate themselves in power as long as they chose. Such a course would also

be in direct opposition to the mandatory provision requiring that trustees, to be annually elected, shall manage the affairs of the company. The enactment (§ 82, R. S. 604) prevents any such arbitrary use of power, and protects stockholders of corporations from the misconduct of their officers in this respect. It imposes a duty upon those officers, in case of a failure to elect, to give notice of another election within a time limited by the section cited. This is in entire harmony with the provisions of the Manufacturing Act, and does not conflict in any way with the right of the officers to make reasonable and prudential rules and regulations for the management and disposition of the stock and business affairs of the company under § 8 of the act. To hold that an election of officers of a corporation must utterly fail because those in power, by accident or design, omit to do their duty, and by neglecting to give the proper notice, or by failing to make proper by-laws for that purpose, would be in contravention of the manifest intention of the law, and sanction a construction entirely unwarranted. No such power was intended to be conferred upon officers of corporations."

⁵ *Brown v. Union Ins. Co.*, 3 La. Ann. 177, 182 (1848). But in those jurisdictions where the common law prevails, the rule is probably otherwise, and a court of equity would not in such a case appoint

§ 607. *The majority of votes cast shall elect.*—It is the well settled rule in corporations having a capital stock divided into shares that a majority of the votes cast at any election shall elect.¹ The minority in such incorporated bodies are under an implied obligation to submit in an election to the will of the majority. This is one of the features which distinguishes a body corporate from a mere private business association.² And this majority, moreover, need not be an actual numerical majority of all the votes which all the stockholders have, but only a majority of the votes cast.³ Accordingly, a majority of the votes cast will elect,

a receiver. *Curry v. Woodward*, 53 Ala. 371, 375 (1875); *Knowlton v. Ackley*, 8 Cush. 93 (1851).

¹ *People v. Albany, &c.*, R. R. Co., 55 Barb. 344 (1869); *East Tennessee, &c.*, R. R. Co. *v. Gammon*, 5 Sneed, 567 (1858); *Dudley v. Kentucky High School*, 9 Bush, 578; *Gifford v. New Jersey, &c.*, R. R. Co., 10 N. J. Eq. 174; *New Orleans, &c.*, R. R. Co. *v. Harris*, 27 Miss. 537; *Treadwell v. Salisbury Manfg. Co.*, 7 Gray, 393. *Cf. Zabriskie v. Hackensack, &c.*, R. R. Co., 18 N. J. Eq. 178 (1867); *Lauman v. Lebanon Valley R. R. Co.*, 30 Penn. St. 42 (1858); *Stevens v. South Devon Ry. Co.*, 9 Hare, 313. In *Durfee v. Old Colony, &c.*, R. R. Co., 5 Allen, 242, Bigelow, C. J., says: "It may be stated as an indisputable proposition that every person who becomes a member of a corporation aggregate, by purchasing and holding shares, agrees, by necessary implication, that he will be bound by all acts and proceedings within the scope of the powers and authority conferred by the charter, which shall be adopted or sanctioned by a vote of the majority of the corporation, duly taken and ascertained according to law. This is a result of the fundamental principle that the majority of the stockholders can regulate and control the lawful exercise of the powers conferred on a corporation by its charter."

² In *Livingstone v. Lynch*, 4 Johns. Chan. 573 (1820), Chancellor Kent says: "The general principle of law is, that in such private associations the majority cannot bind the minority, unless it be by special agreement. Lord Coke (Co. Litt. 181, b) took the distinction between public and private associations, and admitted that in matters of public concern the voice of the majority should govern, because it was for the public good, and the power was to be more favorably expound-

ed than when it was created for private purposes. In *Viner* (tit. Authority B) we have several cases marking the same distinction; and it is now well settled that in matters of mere private confidence, or personal trust or benefit, the majority cannot conclude the minority; but where the power is of a public or general nature, the voice of the majority will control on grounds of convenience; and this is also part of the law of corporations. (*Attorney-General v. Davy*, 2 Atk. 212; *The King v. Beeston*, 3 Term Rep. 592; *Withnell v. Gartham*, 6 Term Rep. 388; *Grindley v. Barker*, 1 Bos. & Pull. 229; *Green v. Miller*, 6 Johns. Rep. 39; 5 Co. 63, a.) In *Lloyd v. Loring* (6 Vesey, 773) there was a suit by three persons on behalf of themselves and all the other members of a lodge of Freemasons, and Lord Eldon observed "that if he considered them as individuals, the majority had no right to bind the minority. One individual has as good a right to possess the property as any other, unless he can be affected by some agreement."

³ *Columbia Bottom Level Co. v. Meier*, 39 Mo. 53 (1866); *Craig v. First Presbyterian Church*, 88 Penn. St. 42 (1878). In this case the court say: "It may be asked, however, What is meant by the majority? Does it mean the concurrence of the major part of those who happen to be present at a regular corporate meeting, or does it mean a concurrence of a majority of the whole body? There is this distinction between a corporate act to be done by a definite number of persons and one to be performed by an indefinite number. In the first case it is to be observed that a majority is necessary to constitute a *quorum*, and that no act can be done unless a majority be present; in the latter, a majority of any number of those which appear may act. And where

even though a majority of the shares of stock are not voted at all, the owners being present at the meeting and refusing to vote.¹

§ 608. *Every share of stock is entitled to one vote.*—At common law, in public or municipal corporations, each qualified elector has one vote, and but one. This rule has been applied to stockholders in a private corporation. And it has been held that such a stockholder is entitled to but one vote, although he be the owner of many shares of the capital stock.² Almost universally, however, the charter of the corporation, or a statute, or a constitutional provision, gives to each share of stock one vote at every corporate meeting, and at the present day it is probable that no court, even in the absence of any such provision, would uphold a rule which disregards, in the matter of voting, the number of shares which the shareholder holds in the corporation.³ The right of the stockholder to vote cannot be taken away or restricted by by-law,⁴ and votes even for a candidate who is disqualified are not wholly to be disregarded in determining the result of the election.⁵ But, in an election of directors, votes which are cast

a corporation is composed of several integral parts, and each part consists of a definite number, a majority of each part must be present to constitute a *quorum*. *St. Mary's Church Case*, 7 Serg. & R. 517. But when a corporation consists of several integral parts, one of which is indefinite, if any number of persons composing the latter, however small, are present after having been duly summoned, it is sufficient. The distinction is between a definite and an indefinite number. In the former case a majority must be present, whereas, in the latter, a majority of those present may act whether a majority of the whole body or not. *Angell & Ames on Corp.*, 464; *Willcock on Mun. Corp.*, 66; *The King v. Whitaker*, 9 B. & C. 648." *s. r. Gowen's Appeal*, 10 Weekly Notes Cas. 85 (1881). See *Commonwealth v. Wickersham*, 66 Penn. St. 134 (1870).

¹ *State v. Green*, 37 Ohio St. 227 (1881). In Pennsylvania there was formerly a contrary rule. *Commonwealth v. Wickersham*, 66 Penn. St. 134 (1870). But see *Gowen's Appeal*, 10 Week. Notes Cas. 85 (1881).

² *Taylor v. Griswold*, 14 N. J. Law, 222 (1834).

³ *Hays v. Commonwealth*, 82 Penn. St. 518 (1876).

⁴ *Brewster v. Hartley*, 37 Cal., 15, 24 (1869); *People v. Kip*, 4 Cowen, 382, note (1822); *Rex v. Spencer*, 3 Burr. 1827 (1766). In *Brewster v. Hartley*, *supra*, the court say: "The power of electing the directors of a railroad corporation is lodged by the statute in the hands of the stockholders. The exercise of this power having been regulated by the statute, the corporation cannot, by its by-laws, resolutions, or contracts, either give or take it away. Where the statute is silent in this respect, the election of the directors, like the election or appointment of subordinate officers, would be subject to the regulation and control of the corporation, but the statute having expressly declared who shall be entitled to vote for directors, its provisions are imperative upon the corporation, constituting a part of the law of its being, and the corporation has no authority to extend or limit the right as regulated by the statute. The first section of the act of 1861 (*Stats.* 1861, p. 607) provides that the first board of directors shall be elected by the stockholders, each stockholder being entitled to one vote for each share of stock which he owned for ten days next preceding such election."

⁵ If the candidates for whom a majori-

for persons who are not and cannot lawfully be candidates, must be thrown out altogether.¹ A statute which confines the right to vote to stockholders who are citizens of the State by which the corporation is chartered is constitutional, and it cannot be evaded by colorable transfers of shares to residents of the State merely for the purpose of having them voted upon.² When a municipal corporation is a stockholder in a private corporation, it is entitled to vote upon its stock in the same way as any other stockholder.³

§ 609. *Cumulative voting.*—In the constitutions of several of the States there are provisions for securing a representation for the minority of the shareholders of incorporated companies upon the board of directors or trustees. This is effected by what is known as a system of cumulative voting. By it each shareholder is entitled to as many votes for directors as the number of shares he owns amounts to when multiplied by the number of directors to be elected. Thus, if there are six directors to be elected, a stockholder who owns one hundred shares, may poll six hundred votes, and these votes he may give entirely to one, or two, or more of the six candidates, as he may see fit. In this way any minority of the stockholders exceeding one sixth part, acting together, might elect one member of a board of six directors and thus secure a representation in that body. A larger minority

ty of the votes for directors was given or offered were disqualified for the office, the court will set aside their election and order a new election; but if they were qualified, and the election was in all respects fairly conducted, except that certain legal votes tendered for them were rejected, leaving them in a minority, the court will set aside the election of the rival candidates, and make an order putting them into their place. In the Matter of Election of St. Lawrence Steamboat Co., 44 N. J. Law, 529 (1882).

¹ Where a meeting was called to elect three directors, and a majority of the stockholders voted for five directors, only a small minority voting for three, the latter votes were held the only valid ones, and the three voted for were declared elected. The court said: "There may be no doubt that the majority of the stockholders in interest were opposed to those declared duly elected, but courts

only respect the will of individuals when it is embodied in the forms required by law. A candidate may receive only ten votes and be elected when there may be hundreds against him who have not expressed their voice in the way the law prescribes. As the stockholders willfully and knowingly voted in disobedience to the resolution under which the election was held, they have no just ground of complaint. It is a matter of importance that offices should be filled, and if electors will knowingly cast their votes in an illegal manner, they cannot object that those elected by the legal vote are not the choice of the majority of those entitled to vote." *State v. Thompson*, 27 Mo. 365, 369 (1858).

² *State v. Hunton*, 28 Vt. 594 (1856).

³ *Kreiger v. Shelby R. R. Co.* (Ky. 1886); 25 Am. & Eng. R. R. Cas. 528. See also § 99, *supra*.

might secure the election of two members of such a board, the possibility of increasing the minority representation increasing as the minority increases, without it ever becoming possible for a minority upon a full vote to secure more than its equitable proportion of the representation. The larger the number of directors, the smaller would be the minority which would be able to elect one member of the board, and the larger the minority the greater the representation possible to be secured. Constitutional provisions which are designed to secure such a minority representation are found in California, Pennsylvania, Illinois, West Virginia, Missouri, and Nebraska.¹ These provisions, if designed to be retroactive, have been held unconstitutional and void. They can only apply to corporations chartered after their enactment.² So far as they concern corporations chartered before the adoption of such a constitutional provision, they impair the obligation of the contract between the corporation, the stockholders, and the State, and infringe the vested rights of the stockholders.³

¹ In California there is the following constitutional provision: "In all elections for directors or managers of corporations every stockholder shall have the right to vote, in person or by proxy, the number of shares of stock owned by him, for as many persons as there are directors or managers to be elected, or to cumulate said shares and give one candidate as many votes as the number of directors multiplied by the number of his shares of stock shall equal, or to distribute them on the same principle, among as many candidates as he shall think fit, and that such directors or managers shall not be elected in any other manner." Constitution of California, 1879, art. XII, § 12. See this provision of the constitution construed in *Wright v. Central California Colony Water Co.*, Sup. Ct. Cal. (1885); 13 Am. & Eng. Corp. Cas. 89.

In Illinois [Constitution of 1870, art. XI, § 3], stockholders in private corporations are allowed "in all elections for directors or managers," "to cumulate shares and give one candidate as many votes as the number of directors multiplied by the number of his shares of stock shall equal, or to distribute them on the same principle among as many candidates as he shall see fit."

In Pennsylvania [Constitution of 1873, art. XVI, § 4], the provision is that "in all

elections for directors or managers of a corporation, each member or shareholder may cast the whole number of his votes for one candidate, or distribute them upon two or more candidates, as he may prefer." See *Wright v. Commonwealth of Pennsylvania* (Sup. Ct. of Penn., 1885), 11 Am. & Eng. Corp. Cas. 609.

In the constitutions of West Virginia [Constitution of 1872, art. XI, § 4], Nebraska [Constitution of 1875, art. XI, miscellaneous provisions § 5], and Missouri [Constitution of 1875, art. XII, § 6], will be found provisions essentially similar to the one in the Constitution of California, *supra*.

² *State v. Greer*, 78 Mo. 188 (1883); *Hays v. Commonwealth*, 82 Penn. St. 518 (1876).

³ In *Hays v. Commonwealth*, 82 Penn. St. 518, 522 (1876), the court, in holding the constitutional provision allowing cumulative voting if it applied to existing corporations, void, as within the constitutional inhibition against impairing the obligation of the contract, said: "Now, whilst it cannot be said that this would not be an alteration in the terms of the charter, it is nevertheless urged that it is a mere regulation of the right of suffrage in corporations, but affected the vested rights of no one. But if it be not a vested right in those who own a major part of the stock of the corporation to elect,

§ 610. *Proxies*.—At common law a stockholder has no right to cast his vote by proxy. This rule was probably evolved from the analogous rule governing municipal corporations, which requires all votes to be given in person.¹ When the charter is silent, the right to vote by proxy may, in the absence of a statutory provision, be conferred by a by-law.² This right is, however, usually secured to stockholders in corporations by statute.³ A proxy should be in writing, but it need not be in any particular form; it need not be acknowledged or proved, but it must be in such a shape as reasonably to satisfy the inspectors of election of its genuineness and validity.⁴ And to this end the corporate officers may insist upon reasonable evidence of the regularity and genuineness of the proxy, before allowing it to be voted.⁵ Where certificates of proxies are destroyed after use, parol evidence is admissible to prove their former existence, and sufficiency.⁶ Proxies are in general presumed to be given in reference to the transaction of the regular, ordinary business of the corporation, and to authorize votes for whatever is within the scope of the usual and legitimate business of the concern. A general proxy, in the usual form, will not therefore authorize a vote to dissolve

if they see proper, every member of the board of directors, I would like to know what a vested right means? This was part of the contract under which they entered into the company, and for which they paid their money." Upon the question of the constitutionality of statutes providing for minority representation, or cumulative voting in the election of public officers, a matter germane to the present subject, see *People v. Kenney*, 96 N. Y. 294 (1884); *People v. Crissey*, 91 Id. 616 (1883); *State v. Constantine*, 42 Ohio St. 437.

¹ *Taylor v. Griswold*, 14 N. J. Law, 223 (1834); *Phillips v. Wickham*, 1 Paige, 590 (1829); *State v. Tudor*, 5 Day (Conn.), 329 (1812); *Brown v. Commonwealth*, 3 Grant (Penn.), 209 (1856); *Craig v. First Presbyterian Church*, 88 Penn. St. 42 (1882); *Commonwealth v. Bringham*, 103 Id. 134 (1883); *People v. Twaddell*, 18 Hun, 427, 430 (1879); *Harben v. Phillips*, L. R. 23 Chan. Div. 14, 22 (1882). *Of. Case of the Dean and Chapter of Farnes, Davies*, 129; *Attorney General v. Scott*, 1 Vesey, 413.

² *People v. Crossley*, 69 Ill. 195 (1873); *Phillips v. Wickham*, 1 Paige, 598 (1829); *State v. Tudor*, 5 Day, (Conn.) 329 (1812).

Chancellor Kent says: "Though in the case of electors in public and municipal corporations, and in all other elections of a public nature, every vote must be personally given, yet in the case of moneyed corporations, instituted for private purposes, it has been held that the right of voting by proxy might be delegated by the by-laws of the institution, when the charter was silent." 2 Kent's Commentaries, 294, 295. This is denied in New Jersey. *Taylor v. Griswold*, 14 N. J. Law, 222 (1834).

³ N. Y. Session Laws, 1850, chap. 40, § 5. In New York a statute forbids the buying or selling of proxies for the purpose of voting railroad stock. New York Session Laws, 1880, chap. 510.

⁴ In the Matter of Election of St. Lawrence Steamboat Co., 44 N. J. Law, 529 (1882).

⁵ Id.

⁶ *Haywood & Pittsburgh Plank Road Co. v. Bryan*, 6 Jones (N. C.), 82 (1858). Where one gave a proxy to vote at an annual election, it was held *prima facie* evidence that he was a stockholder just before such election. *Harger v. McCullough*, 2 Denio, 119, 122 (1846).

the corporation, or to sell the entire corporate property and business.¹ And an irrevocable power of attorney, or proxy, authorizing a vote upon stock, is not contrary to public policy, though the owner reserves the power of transfer.²

But a written contract not to vote by proxy, entered into by certain shareholders mutually for the purpose of preventing the board of directors from consummating a proposed sale of the franchises of the corporation, was held a pernicious and unlawful compact.³

§ 611. *The transfer book as evidence of a right to vote.*—The question who is entitled to vote upon a particular share of stock is, as a general rule, answered by a reference to the corporate transfer book; he who is there registered as the owner of the stock is entitled to vote upon it.⁴ It is not necessary that the owner of stock produce his certificate, or even have a certificate, in order to vote.⁵ Neither will indebtedness for the subscription price prevent the stockholder from voting.⁶ So also it is immaterial that the person in whose name the stock is reg-

¹ *Abbot v. American Hard Rubber Co.*, 33 Barb. 578, 584 (1861). In the opinion in this case, Josiah Sutherland, J. vigorously said: "In passing the resolution relied upon by the defendants as an authority, by a majority of the stockholders, to make the sale and transfer, it would appear that a majority of shares voted on were voted on by proxy. I must presume, in the absence of anything to show the contrary, that these proxies were ordinary proxies, given with reference to the transaction of the ordinary legitimate business of the corporation, and that they did not and could not authorize votes for so extraordinary a sale and transfer as the one in question. Hence, the resolution cannot be said to have been, in fact, passed by a majority of the stockholders, and its passage can hardly be claimed as an authority by a majority."

"A similar remark may be made as to the Connecticut statutes referred to by the counsel for the defendants, authorizing a majority of the stockholders to transact business, and not less than three directors to manage the affairs and business of the corporation; these statutes must be presumed to have been intended to apply to the ordinary and legitimate business and affairs of corporations, and

not to so extraordinary a proceeding as the sale and transfer in question." See also 21 How. Prac. 193; 11 Abb. Prac. 204; and *cf.* *Cumberland Coal Co. v. Sherman*, 30 Barb. 533 (1859).

² *Brown v. Pacific Mail Steamship Co.*, 5 Blatchf. 525 (1867).

³ *Fisher v. Bush*, 35 Hun, 641 (1885).

⁴ In the *Matter of the Long Island R. Co.*, 19 Wend. 37, 44 (1837), the court saying: "The votes upon the stock standing in the name of D. J., were properly received. The inspectors were not to inquire beyond the transfer book (1 R. S. 608, § 6). Any private agreement or understanding between the individual holding the legal title to the stock in due form, and others, is a matter between themselves with which the corporation have no concern." *Ex parte Willcocks*, 7 Cowen, 402 (1827); *State v. Ferris*, 42 Conn. 560, 568 (1875).

⁵ *Beckett v. Houston*, 32 Ind. 393 (1869).

⁶ *Birmingham, &c., Ry. Co. v. Locke*, 1 Q. B. 256 (1841); *Savage v. Ball*, 17 N. J. Eq. 142 (1864); *Downing v. Potts*, 23 N. J. Law, 66 (1851). So held in this case, even though the subscriber had paid nothing on his stock.

istered is merely the nominal holder, and that another person really owns the stock.¹ A subscriber upon a condition not yet performed may vote upon the question whether that condition shall or shall not be performed.² And stock issued for construction, the work not having been performed, may nevertheless be voted.³ In New York, by statute, the corporate transfer book is made conclusive upon the question who may vote.⁴ But no person is allowed to vote upon railroad stock which he has sold, whether the transfer has been registered or not.⁵ And in moneyed and railway corporations only those stockholders are entitled to vote who have been duly recorded as stockholders for thirty days previous to the election.⁶ Substantially similar provisions are to be found in the statutes of other States.⁷ In the absence of statutory provisions to the contrary, the weight of authority favors the rule, that although a stockholder has sold his stock and transferred the certificate, yet until such transfer has been duly recorded on the corporate books, he is entitled to vote upon the stock.⁸ But in

¹ Under the Nevada statutes a person who *holds* stock, issued in his name, is recognized as a shareholder as well as one who *owns* shares. So, where a father transferred stock to his son to make him eligible to a corporate office, the son paying nothing for the stock, it was held that the son was a stockholder, and might vote the stock. *State of Nevada v. Leete*, 16 Nev. 242 (1881).

² *Greenville, &c., R. R. Co. v. Coleman*, 5 Rich. Law, 118 (1851).

³ *Savage v. Ball*, 17 N. J. Eq. 142 (1864).

⁴ 1 Rev. Stat. of New York, chap. XVIII, title IV, § 5; *Vandenburgh v. Broadway Railway Co.*, 29 Hun, 348, 355 (1883); *In the Matter of the Long Island R. R. Co.*, 19 Wend. 37 (1837); *In the Matter of the Mohawk & Hudson R. R. Co.*, Id. 135 (1838). But see *Strong v. Smith*, 15 Hun, 222 (1878).

⁵ New York Session Laws, 1880, chap. 510.

⁶ 1 Rev. Stat. of New York, chap. XVIII, title II, art. 2, §§ 38, 45. Also as to Railway Corporations, New York Laws of 1850, chap. 140, § 5.

⁷ *Downing v. Potts*, 23 N. J. Law, 66 (1851). *In the Matter of the Election of St. Lawrence Steamboat Co.*, 44 Id. 529 (1882); *Hoppin v. Buffum*, 9 R. I. 513 (1870). See for the English rule, *Pender v. Lushington, L. R.*, 6 Chan. Div. 70

(1877), where the court says: "How are you to ascertain who is to vote? That is pointed out by the articles of association. First, who are to be summoned to attend the general meetings? You find by article 48, that notice is to be given to 'the members hereinafter mentioned.' What does the word 'members' mean in that article? The definition clause, like many other definition clauses, is one which defines nothing. It says, 'Member means member for the time being of the company,' that is, member means member. But one must remember that the word 'member' has a meaning in the Companies Act, and it means *prima facie* a registered shareholder or stockholder, and that must be the meaning here, because how else are you to give him notice at all? You can only give him notice by referring to the register which, under Article 2, is 'to be kept pursuant to terms of the Companies Act, 1862. So that a member is a man who is on the register.'"

⁸ *McNeil v. Tenth National Bank*, 46 N. Y. 325, 332 (1871). *In the Matter of the Long Island R. R. Co.*, 19 Wend. 37 (1837); *People v. Robinson*, 64 Cal. 373 (1883); s. c. 1 Pac. Rep. 156 (1883); *Mousseaux v. Urquhart*, 19 La. Ann. 482 (1867); *State v. Ferris*, 42 Conn. 560 (1875); *State v. Pettineli*, 10 Nev. 141 (1875); *Johnston v. Jones*, 23 N. J. Eq.

Illinois it is held that the corporation must allow the real owner of the stock to vote, whether he be the registered owner or not.¹ The corporation may be compelled to register transfers made merely for the purpose of voting,² while colorable transfers made solely to enable the fictitious transferees to enjoy certain privileges, which it is the intent of the charter provision conferring them, that only *bona fide* stockholders shall enjoy, will be set aside as unwarranted by a court of equity.³

A by-law allowing election inspectors to administer an oath to the voters at a corporate election, and to interrogate the stockholders who offer their votes, under such oath, is illegal and void.⁴ In general, as has been shown, each share of stock is entitled to one vote, but under certain circumstances the holders of scrip issued as a dividend are not entitled to the right to vote upon such stock.⁵ This is not, however, the rule as regards a stock dividend, and it is generally conceded that the holders of stock

216, 228 (1872); *Downing v. Potts*, 28 N. J. Law, 66 (1851); *Hoppin v. Buffum*, 9 R. I. 513 (1870). *Of* In the Matter of the North Shore Staten Island Ferry Co., 63 Barb. 556 (1872); *Smith v. American Coal Co.*, 7 Lans. 317 (1873). In *People v. Robinson*, *supra*, the court, at p. 375, well say: "A transfer not entered on the books of the company has no validity outside of the parties to such transfer. If not, could it affect the validity of an election at which trustees of the company were elected? If so, would not a transfer, although not entered on the books of the company, be valid outside of the parties to such transfer? The construction which we feel compelled to give to this clause is, that a transfer of stock, until entered upon the books of the company, confers on the transferee, as between himself and the company, no right beyond that of having such transfer properly entered. Until that is done, or demanded to be done, the person in whose name the stock is entered on the book of the company is, as between himself and the company, the owner to all interests and purposes; and particularly for the purposes of an election."

¹ *People v. Devin*, 17 Ill. 84 (1855). This is not a satisfactory position and might not now be followed. See also *Allen v. Hill*, 16 Cal. 113 (1860).

² In *re Stranton Iron & Steel Co.*, L. R., 16 Eq. 559 (1873).

³ It is provided by the charter of the Academy of Music in Philadelphia, that every five shares of stock shall entitle the owner to a free ticket of admission, and that the directors shall set apart a portion of the house for the exclusive use of such stockholders. Certain stockholders owning large blocks of the stock were in the habit of transferring lots of five shares each to other persons at the opening of the season, to be retransferred to them again at its close. Upon a bill filed by certain stockholders to restrain such fictitious transfers, the court held that the transfers were not warranted, and that costs should go against the corporation for permitting such transfers. *Appeal of the Academy of Music*, 108 Penn. St. 510 (1885).

⁴ *People v. Kip*, 4 Cowen, 382, note (1822).

⁵ Where the New York Central Railroad Co., issued what were denominated "interest certificates," which were practically certificates of stock issued as a scrip dividend, except that they were payable at the pleasure of the company out of its future earnings, and convertible, upon certain conditions, into the common stock of the company, it was held that the holder of such certificates were not entitled to vote upon them at corporate elections. *Bailey v. Railroad Company*, 22 Wall. 604, 635 (1874).

issued as a stock dividend, or the holders of preferred stock, stand, in respect of the right to vote upon their shares, precisely upon the same footing as the holders of the common stock of the corporation.¹ In New York, when for any reason the corporation fails to hold an election at the stated time as provided in the charter or by-laws, and the election is held subsequently, only those stockholders are entitled to vote who were qualified electors at the time when the election ought to have been held.² •

§ 612. *The right of trustees, pledgees, married women, administrators, &c., &c., to vote.*—It is the general rule that a person holding stock as trustee, not only where he is duly registered as a stockholder in that capacity, but also where the trust relationship is not declared upon the books of the corporation, is entitled to vote upon the stock.³ It seems, however, that in case of a trust not coupled with an interest, and where the *cestui que trust* could, by bill in equity, compel a conveyance of the property to himself, he might compel the trustee to vote as he directed.⁴ In New York a statute enables a married woman to vote in person or by proxy on any shares of stock she may own.⁵ So also a duly qualified executor or administrator may vote on stock of his testator or intestate even though such stock has not been transferred on the book.⁶ Although a person pledges stock as collateral security for the payment of a debt or for any other purpose, he is nevertheless entitled to vote upon it at all cor-

¹ "As a general rule stock dividends, even when they represent net earnings, become at once a part of the capital of the company, and of course entitle the holder to vote, unless it is otherwise provided in the charter or by-laws." *Bailey v. Railroad Co.*, 22 Wall. 604, 637 (1874).

² 1 Rev. Stat. of New York, chap. XVIII, title IV, § 8.

³ *Widow Conant v. Millaudon*, 5 La. Ann. 542 (1850); *Wilson v. Proprietors of Central Bridge*, 9 R. I. 590 (1870); *Hoppin v. Buffum*, 9 Id. 513 (1870); *Crease v. Babcock*, 10 Metc. 525, 545 (1846); *In re Barker*, 6 Wend. 509 (1831); *In the Matter of the Mohawk and Hudson R. R. Co.*, 19 Id. 135 (1838); *In the Matter of the North Shore Staten Island Ferry Co.*, 63 Barb. 556 (1872); *Ex parte Holmes*, 5 Cowen, 426 (1826); *Pender v. Lushington*, L. R., 6 Chan. Div. 70 (1877).

⁴ *Hoppin v. Buffum*, 9 R. I. 513

(1870); *Wilson v. Proprietors of Central Bridge*, Id. 590 (1870); *Brewster v. Hartley*, 37 Cal. 15 (1869). *Cf. Stewart v. Mahoney Mining Co.*, 54 Cal. 149 (1880); *Ex parte Holmes*, 5 Cowen, 426, 435 (1826). For the rule as to a trustee of stock for the corporation itself, see § 613.

⁵ New York Session Laws, 1851, chap. 521.

⁶ In the *Matter of the North Shore Staten Island Ferry Co.*, 63 Barb. 556 (1872); *Middlebrook v. Merchants Bank*, 3 Keyes (N. Y.), 135 (1866). The provision of the New York Manufacturing Cos. Act of 1848, is, viz.: "Every such executor, administrator, guardian, or trustee, shall represent the share of stock in his hands at all meetings of the company, and may vote accordingly as a stockholder." New York Laws of 1848, chap. 40, § 17.

porate meetings so long as it is not transferred into the name of the pledgee.¹ And where the stock has been transferred on the corporate books into the name of the pledgee, it is held that, even then, it cannot be voted contrary to the wishes and interests of the pledgor.² A court of equity will compel the pledgee under some circumstances, when the stock has been transferred, to give the pledgor a proxy;³ but will not, upon the application of the pledgor, enjoin the pledgee from voting, unless it appears that irreparable injury is threatened, and that the pledgor is in danger of loss without an adequate remedy at law.⁴ A partner may properly vote upon stock belonging to the firm, and registered in the partnership name;⁵ so also it seems where the stock belongs to the firm, but is registered in the name of the other partner who is dead.⁶ Where the word "cashier" is added to the name of a shareholder upon the corporate stock book, it is not sufficient to raise a trust, nor will the election of another person to the office of cashier of the corporation operate to transfer the right to vote the stock from the outgoing to the incoming official. The appended word is merely a word of description.⁷

¹ *In re Barker*, 6 Wend. 509 (1831); *Ex parte Willcocks*, 7 Cowen, 402 (1827); *Matter of Cecil*, 36 How. Prac. 477 (1869); *Smith v. American Coal Co.*, 7 Lans. 317 (1873); *Vowell v. Thompson*, 3 Cranch C. C. 428 (1829); *Schofield v. Union Bank*, 2 Id. 115 (1815); *McDaniell v. Flower Brook Manfg. Co.*, 22 Vt. 274 (1850); *Crease v. Babcock*, 10 Metc. 525, 545 (1846); *Hoppin v. Buffum*, 9 R. I. 513 (1870); *Brewster v. Hartley*, 37 Cal. 15 (1869). The provision of the New York Manufacturing Cos. Act of 1848 is viz.: "Every person who shall pledge his stock as aforesaid may nevertheless represent the same at all such meetings, and may vote accordingly as a stockholder." New York Laws of 1848, chap. 40, § 17.

² *Lawrence v. Maxwell*, 53 N. Y. 19 (1873); *Ex parte Willcocks*, 7 Cow. 402, 410 (1827); *Vowell v. Thompson*, 3 Cranch C. C. 428 (1829); *Schofield v. Union Bank*, 2 Id. 115 (1815); *Story on Bailments* (9th edition), § 89; 1 *Schouler on Personal Property* (2d edition), § 435; *Redfield on Carriers*, § 659; *Lewis on Stock-Brokers*, 120; *Stephens on Joint Stock Companies* (Canadian), 401. Cf. *McDaniels v. Flower Brook Manfg. Co.*, 22 Vt. 274 (1850). See also *Fanning v.*

Hibernia Insurance Co., 37 Ohio St. 339 (1881). It is not a conversion for one who holds stock as pledgee, to attend corporate meetings and vote upon the stock, especially where it appears that the president of the company who knew that he held the stock as collateral security, asked him to attend the meeting and to vote. *Heath v. Silverthorn Lead Mining, &c., Co.*, 39 Wis. 146 (1875).

³ *Vowell v. Thompson*, 3 Cranch C. C. 428 (1829).

⁴ *McHenry v. Jewett*, 90 N. Y. 58 (1882). In order to settle a contest growing out of a disputed election, the court may go behind the entry in the transfer book to determine whether a transfer appearing thereon was a sale or only a pledge of the shares, and whether the pledgor or pledgee be entitled to vote thereon. *Strong v. Smith*, 15 Hun, 222 (1878).

⁵ *Kenton Furnace Railroad and Manfg. Co. v. McAlpin*, 5 Fed. Rep. 737 (1880). See *Hardy v. Norfolk Manfg. Co.*, 80 Va. 404 (1885).

⁶ *Allen v. Hill*, 16 Cal. 113 (1860).

⁷ In the *Matter of the Mohawk & Hudson R. R. Co.*, 19 Wend. 135, 146 (1838).

§ 613. *The corporation cannot vote upon shares of its own stock.*—Shares of stock owned by the corporation itself cannot be voted either directly by the corporate officers, or indirectly by a trustee of the corporation. This is the established rule, whether the stock is registered in the name of the corporation or not.¹ The inspectors of election may lawfully inquire into the ownership of stock registered in the names of the directors of the corporation, if there be any reason to suspect that the corporation owns it.² Directors elected by votes upon stock

¹ *Mousseaux v. Urquhart*, 19 La. Ann. 482 (1867); *Vail v. Hamilton*, 85 N. Y. 453 (1881); *Ex parte Holmes*, 5 Cowen, 426 (1826); *McNeely v. Woodruff*, 13 N. J. Law, 352 (1833); *American Railway Frog Co. v. Haven*, 101 Mass. 398 (1869); *State v. Smith*, 48 Vt. 266 (1876); *United States v. Columbian Ins. Co.*, 2 Cranch C. C. 266 (1821); *New England Mutual, &c., Ins. Co. v. Phillips* (Mass. 1886), 13 Am. & Eng. Corp. Cas. 104. *Cf.* *Taylor v. Miami Exporting Co.*, 6 Ohio, 176 (1833); *Frazer v. Whalley*, 2 Hem. & M. 10 (1864). Where shares are bought in by the corporation for non-payment of assessments, the treasurer of the company may vote upon such stock at a meeting where all the stock is represented and all consent to the vote. *Farwell v. Houghton Copper Works*, 8 Fed. Rep. 66 (1881). *Cf.* *Stephens on Canadian Joint-Stock Companies*, 354. In *American Railway Frog Co. v. Haven*, *supra*, the court says, at page 402: "The case finds that the capital stock was divided into two thousand shares, all of which were properly issued to the original stockholders; and that sometime afterwards, four hundred of these shares were transferred by some of the stockholders to Aaron W. Clark, 'to hold for the benefit of the corporation.' If these transfers had been made directly to the corporation, without the intervention of a trustee, it would hardly be contended that it would thereby become entitled to vote at a meeting of stockholders. A corporation cannot literally be one of its own stockholders in the full sense of that term. Such a transfer might not operate as a mere surrender or cancellation of stock unless so intended. It would not diminish the amount of the capital, nor necessarily reduce the number of shares. The corporation might, perhaps, receive such a transfer, and hold the stock so conveyed to it, for the purpose of reissue to new subscribers or pur-

chasers. By the terms of the transfer, Clark holds 'for the benefit of the corporation,' and, of course, subject to its order. This is the extent of his trust. Nothing in the nature of it makes it necessary that he should vote, as the holder of those shares. There is no apparent reason why he, not being beneficially or practically the owner of them, should be endowed with the privilege of controlling four hundred votes according to his own judgment or pleasure, especially when it is taken into consideration that the corporation for which he holds them has no right of voting in any event. It is easy to see that any such privilege would not only be unreasonable and unfair, but might lead to great abuses. The position of these shares, in our judgment, is the same, to all intents and purposes, so far as the right of voting upon them is concerned, as if they were held directly by the corporation itself; and until they are sold and transferred by its authority, the right of voting upon them is suspended."

² *Ex parte Holmes*, 5 Cowen, 426 (1826). The court in this case said "But the question remains, whether the latter are to be deemed stockholders, within the spirit of the act. True, the stock on which they voted, in this case, stands in their name; but, on the face of the entry, they are declared to be mere nominal holders. The real owner of the stock should vote, especially where his name is truly expressed in the books; though it might be otherwise if he choose to have the entry simply in the name of another, without expressing any trust. Now these three persons, a majority of whom claim a right to vote, are mere trustees; and they are trustees, not for the directors but the company, the corporation itself. If there could be a vote at all upon the stock, one would suppose that it must be by each stockholder of

owned by the corporation are illegally elected,¹ and *mandamus* lies to oust directors so elected.² The court may also, in the exercise of its equity powers, declare a candidate elected who received only a minority of the votes actually cast, when such candidate plainly received a majority of all the legal votes cast.³ And a new election will not be ordered where the person declared elected had a majority of legal votes, though not a majority of all the votes, legal and illegal, that were cast at the election.⁴

§ 614. *Injunction against voting particular stock.*—Under certain circumstances it seems that a court of equity might enjoin a stockholder from voting on particular stock. Such an injunction can only issue when the complainant can show a plain purpose of parties to vote the stock, and to vote it in a particular way; that the effect of the vote will be to control the election; that mischief will result to the corporation; and that irreparable or permanent injury will come either to the corporation itself or to the other stockholders.⁵ So, also, where a combination or conspiracy can be shown for the purpose of controlling an election in fraud of the rights of those shareholders who are not in the combination,

the company, in proportion to his interest in it.

"This brings us to the important difficulty in the case; which is, whether stock thus held can vote at all. And we think it is not to be considered as stock held by any one for the purpose of being voted upon. No doubt the company may, from necessity as in this case, take their own stock in pledge or payment; and keep it outstanding in trustees, to prevent its merger; and convert it to their security. But it is not to be voted upon within the meaning of the charter, or general act upon which we are proceeding. It is not to be tolerated, that a company should procure stock in any shape, which its officers may wield to the purpose of an election; thus securing themselves against the possibility of removal."

¹ *Ex parte Desdoits*, 1 Wend. 98 (1828).

² *American Railway Frog Co. v. Haven*, 101 Mass. 398 (1869).

³ *Mousseaux v. Urquhart*, 19 La. Ann. 482 (1867).

⁴ *McNeely v. Woodruff*, 13 N. J. Law, 352 (1833); *Ex parte Desdoits*, 1 Wend. 98 (1828).

⁵ In *Reed v. Jones*, 6 Wis. 680 (1858), where there had been alleged overissue

of stock, upon which the holders proposed to vote, an injunction was denied, but in the opinion the court said: "Now upon general principles it would seem improper and most mischievous to grant an injunction, upon the complaint of a minority of a board of directors, to restrain a stockholder from voting upon an alleged excess of stock, held by him before the company had taken any steps to cancel the stock or declare it void. We have not been referred to any case where an interposition of the court by injunction has been exercised for such a purpose, and after some research, we have been able to find none. But from the allegations of this complaint, it is not easy to perceive how it would produce irreparable and permanent injury to the company or the plaintiffs, even if Jones should vote upon this alleged excess of stock. The complaint fails to show that imminent danger to the property of the plaintiffs is threatened by the contemplated acts; nor does it present any other sufficient ground or reason for arresting and restraining him from voting upon this stock." From this it may be inferred that under other circumstances the injunction would have been allowed.

the injunction will issue.¹ Such an injunction will not prevent an election from taking place. On the contrary, the election goes on, and is valid even though it happen that, what would have been a minority of the votes, had not the injunction issued, becomes, by reason thereof, a majority, and elects.² The general rule, however, unquestionably is, that one stockholder has nothing to do with the vote of another stockholder, and can lawfully do nothing to abridge the right of another to vote, or to control or direct the casting of the vote of any other member of the corporation.³

Accordingly, an injunction will not be granted upon the ground that the stockholders against whom the injunction is sought, are likely to obtain control of the affairs of the company, and that then they will probably misuse their power.⁴ Nor will an injunction be allowed where the application is made for it at such a time that, according to the rules of practice, the defendants cannot be heard in opposition to it until after the day of election; so that the operation of the injunction would be the same, whether the court at the hearing granted it or denied it. It is held that such an application ought to be summarily dismissed.⁵

§ 615. *Illegal or fraudulent elections.—Shareholders' remedies herein.*—There are various ways in which an illegal or fraudulent election of directors or managers of an incorporated company can be investigated, the fraud unearthed, and the illegality set aside. At common law, the action of *quo warranto*, in the name of the State, upon the relation of the parties aggrieved, will lie upon probable cause shown to try the title of the candidate who claims an election. The statutes of the several States

¹ Webb v. Ridgely, 38 Md. 364 (1873); Brown v. Pacific Mail Steamship Co., 5 Blatchf. 525 (1867); People v. Albany & Susquehanna R. R. Co., 55 Barb. 344 (1869); Hafer v. New York, &c., R. R. Co. (Ohio), 14 Week. Law Bul. 68 (1885). See Hoppin v. Buffum, 9 R. I. 513 (1870); Griffith v. Jewett (Ohio), 15 Week. Law Bul. 419 (1886).

² Brown v. Pacific Mail Steamship Co., *supra*.

³ Ryder v. Alton, &c., R. R. Co., 13 Ill. 516 (1851).

⁴ Camden, &c., R. R. Co. v. Elkins, 37 N. J. Eq. 273 (1883).

⁵ Where a bill was filed to restrain certain shareholders from selling or assigning their stock, or from voting upon it at an ensuing election, which was to be held within three days from the dates of the filing of the bill, the court held that inasmuch as the probable effect of the injunction would be to change the result of the election, and the consequent control of the affairs of the company, without allowing the shareholders sought to be restrained, to be heard in their own defense, the injunction ought to be denied. Hilles v. Parish, 14 N. J. Eq. 380 (1862).

will in general be found to prescribe an action in such cases in the nature of the older common law action of *quo warranto*, and under these statutes this is still a common remedy.¹

In comparatively recent times, a concurrent remedy has been provided in a court of chancery. While it is true, as a general proposition, that such a court has no jurisdiction to try or determine the validity of a corporate election,² unless such jurisdiction is conferred by statute, nevertheless, whenever the question arises incidentally in connection with a suit in which a court of equity has jurisdiction, the legality or validity of an election may be passed upon,³ and it has been held that fraud will give a court of equity jurisdiction to set aside an election of directors.⁴ And where the process of a court has been unlawfully or unjustly used to control a particular election, the proceedings in court being dropped immediately after the election, all the acts done, by virtue of such control, being in fraud of the rights of the shareholders, will be summarily vacated and set aside,⁵ and it has been held that upon general principles of equity jurisprudence, and irrespective of statutory provision, the shareholders in a private corporation have such a pecuniary interest in its affairs as will give them standing in a court of chancery, to try the validity and regularity of an election of directors, and the legality of the acts of inspectors in receiving or rejecting votes, and declaring the result.⁶

¹ There cannot be such a thing as a *de facto* officer as against the people in an action at the suit of the people to try the title of the office. The doctrine of officers *de facto* applies only to and in favor of third persons, and to protect innocent parties who have trusted to the apparent title of an officer. *The People v. Albany, &c., R. R. Co.*, 55 Barb. 344, 385 (1869). *Cf. Ex parte Willcocks*, 7 Cowen, 402 (1827); *Boardman v. Halliday*, 10 Paige, 228; *The People v. Albertson*, 8 How. Prac. 363 (1853); *Weeks v. Ellis*, 2 Barb. 325. And see particularly *Mechanics National Bank of Newark v. Burnet Mfg. Co.*, 32 N. J. Eq. 236 (1880).

² *Mickles v. Rochester City Bank*, 11 Paige, 118 (1844); *Mechanics National Bank of Newark v. Burnet Mfg. Co.*, 32 N. J. Eq. 236 (1880); *Johnston v. Jones*, 23 Id. 216 (1872); *Owen v. Whitaker*, 20 Id. 122 (1869). *Cf. Wandsworth, &c., Gas Light & Coke Co. v. Wright*, 18 W.

R. 728 (1870); *Beecher v. Wells' Flouring Mill Co.*, 1 Fed. Rep. 276 (1880); s. c. 1 McCrary, 62.

³ *Mechanics National Bank, &c. v. Burnet Mfg. Co.*, 32 N. J. Eq. 236 (1880); *Johnston v. Jones*, 23 Id. 216 (1872).

⁴ *Davidson v. Grange*, 4 Grant's Chan. (Up. Can.) 377 (1854); *Wandsworth, &c., Gas Light & Coke Co. v. Wright*, 18 W. R. 728 (1870), where the court said: "*Prima facie* the persons declared elected were directors. If this had been done by means of a conspiracy, this court would have found its arm long enough to deal with such a fraud."

⁵ *Putnam v. Sweet*, 1 Chandler (Wis.), 286 (1849). *Cf. People v. Albany & Susquehanna R. R. Co.*, 55 Barb. 344 (1869).

⁶ In the Matter of Election of St. Lawrence Steamboat Co., 44 N. J. Law, 529 (1882). But see *New England Mutual, &c., Ins. Co. v. Phillips* (Mass. 1886), 13 Am. & Eng. Corp. Cas. 104.

In many of the States, statutes have been enacted which give courts of equity the power to review corporate elections at the instance of the parties aggrieved.¹ In New York, the Supreme Court setting as a court of chancery, is empowered to review corporate elections, and to grant such relief as the particular circumstances and justice of the case seem to require.² Under these statutes an election may be declared void by reason of the conspiracy, frauds, or trickery of a part of the corporators.³

§ 616. But only a shareholder whose rights have been infringed and who is equitably entitled to complain, may institute the proceedings. Accordingly a transferee of one of the shareholders who participated in the fraud will not be heard to impeach the result of that fraud.⁴ And in general the plaintiff, a relator seeking to set aside a corporate election, is barred of relief if he himself was guilty of misconduct or neglect, or if it appears that he has subsequently acquiesced with knowledge of the facts.⁵ It is a principle of law also that the legality of an election will not be inquired into upon the ground that illegal votes were cast, unless those votes were challenged at the election at the time when they were cast.⁶ Neither can an election be successfully contested if it be shown that after throwing out the invalid votes the officers declared elected would still have a valid majority of the votes cast according to the return.⁷ But if it appear that

¹ Statutes of California, 1876, § 5315; *Brewster v. Hartley*, 37 Cal. 15 (1869). *Cf. Wright v. Central California Colony Water Co.*, Sup. Ct. Cal., 1885, 13 Am. & Eng. Corp. Cas. 89.

² 1 Rev. Stat. chap. XVIII, title IV, § 5 (page 603); title II, art. second, §§ 47-50 (page 598); *The Schoharie Valley R. R. Case*, 12 Abb. Prac. (N. S.) 394 (1872).

³ *People v. Albany, &c.*, R. R. Co., 55 Barb. 344 (1869).

⁴ *Matter of the Application of the Syracuse, &c. R. R. Co.*, 91 N. Y. 1 (1883).

⁵ *Wiltz v. Peters*, 4 La. Ann. 339 (1849).

⁶ In the *Matter of the Chenango, &c. Ins. Co.*, 19 Wend. 635 (1839), wherein the court said: "It is quite clear, generally speaking, that an illegal vote, not challenged, will not invalidate an election, nor will even be inquired into." *Cf. The Schoharie Valley R. R. Case*, 12 Abb. Prac. (N. S.) 394 (1872).

⁷ *People v. Tuthill*, 31 N. Y. 550 (1864); *Ex parte Murphy*, 7 Cowen, 153 (1827); In the *Matter of the Chenango, &c. Ins. Co.*, 19 Wend. 635 (1839); *State v. Lehre*, 7 Rich. (Law), 235, 325 (1854); *McNeely v. Woodruff*, 13 N. J. Law, 352 (1833); *First Parish in Sudbury v. Stearns*, 21 Pick. 148 (1838); *Trustees of the School District v. Gibbs*, 2 Cush. 39 (1848); *Wardens of Christ Church v. Pope*, 8 Gray, 140 (1857). Where it appeared that there were two illegal votes cast in a poll of thirty-seven, the candidates declared elected having received twenty-one votes, including the two irregular ones, the court held that the election must stand, saying: "Rejecting, therefore, the two votes which were held to have been improperly received by the general term, the incumbents have still a majority of presumptively legal votes. The election is not to be set aside and declared void merely because two votes were received from persons not entitled

the person declared elected did not have a clear majority of all the legal votes cast he will be ousted.¹ The courts are not agreed upon the question whether a person under such circumstances, who received only a minority of all the votes actually cast, but a majority of the votes which were lawfully cast, may be declared elected. In some cases it is held that a candidate who receives a majority of lawful votes is elected, without reference to the number of illegal votes cast against him.² But in others it is said that the court will merely order a new election.³

§ 617. *Injunctions against elections.*—An injunction will in certain cases as has been shown⁴ be granted to prevent a vote upon particular shares of stock, but an injunction forbidding the holding of any election whatever is an interference with the management of corporate affairs to which the courts will decline to be a party, and such an injunction would if granted be void.⁵

§ 618. *Combinations and contracts as to elections.*—Stockholders owning a majority of the stock have a right to combine and secure the election of the board of directors,⁶ provided it be done without fraud in forming the combination,⁷ and a contract to sell one's stock in a corporation, and to resign a directorship and the presidency, and having done so to endeavor to induce other directors to resign, in order that the purchasers of the stock may come in and take their places and so obtain influence in the management of the concerns of the company, where there was no evidence of fraud, has been held a contract not void as against public policy.⁸ But a contract made by a stockholder for a con-

to vote if there was still a majority of legal votes for the ticket declared to be elected." *People v. Tuthill*, *supra*, p. 563.

¹ *People v. Devin*, 17 Ill. 84 (1855).

² *State v. Swearingen*, 12 Ga. 23 (1852); *In the Matter of Election of St. Lawrence Steamboat Company*, 44 N. J. Law, 529 (1882); *Mousseaux v. Urquhart*, 19 La. Ann. 482 (1867); *Ex parte Desdoity*, 1 Wend. 98 (1828). See *In the Matter of the Long Island R. R. Co.*, 19 Wend. 37 (1837). *Cf. Downing v. Potts*, 23 N. J. Law, 66 (1851).

³ *State v. McDaniel*, 22 Ohio St. 354 (1872); *People v. Phillips*, 1 Denio, 388 (1845); *In the Matter of the Long Island R. R. Co.*, 19 Wend. 37 (1837).

⁴ § 614, *supra*.

⁵ *People v. Albany, &c. R. R. Co.*, 55 Barb. 344 (1869). *Cf. New England Mutual, &c. Ins. Co. v. Phillips* (Mass. 1886), 13 Am. & Eng. Corp. Cas. 104, where it is held that a bill in equity for an injunction cannot be maintained for the purpose of determining the question of the contested election of the directors of a railway company.

⁶ *Havemeyer v. Havemeyer*, 43 N. Y. Super. Ct. 506, 513 (1878); s. c. affirmed, 86 N. Y. 618 (1881); *Barnes v. Brown*, 80 N. Y. 527, 537 (1880); *Faulds v. Yates*, 57 Ill. 416 (1870).

⁷ *People v. Albany, &c. R. R. Co.*, 55 Barb. 344 (1869). See *Fisher v. Bush*, 35 Hun. 641 (1885).

⁸ *Barnes v. Brown*, 80 N. Y. 527

sideration, to vote for a particular person for manager of the company and, in the event of his election, to vote for an increase of the salary attaching to that position, is illegal and cannot be enforced.¹ The right to vote upon stock cannot, however, be denied or abridged because of alleged wrongful motives influencing the holder in buying and holding the stock.² And a compact whereby the holders of a majority of the stock in a railway corporation, in exchange for transferable trust certificates, transfer their shares to a board of trustees, who take the legal title to the stock, receive the dividends and account to the equitable owners, and vote upon the stock at corporate meetings, the object of the arrangement being to prevent other parties from gaining a controlling interest in the company, and to secure the property from an anticipated lease to another corporation, is not illegal nor contrary to public policy.³

(1880). In this case the president of a company who owned a controlling interest in the stock, entered into a formal contract with two persons who desired to become stockholders, to sell to them all his stock, to resign the presidency and a directorship, and to use his influence to get other directors to resign, to the end that his two vendees might come in and assume the control of the corporate affairs. Of this contract the court say: "There was nothing in the written contract between the parties which required the plaintiff to transfer the control and management of the corporation to Brown and Seligman; but I will assume that it was the understanding and a part of the scheme that he should do so. Brown and Seligman were attempting to procure the control of the corporation and of its franchises for a legitimate purpose. There is no reason to suppose that they meant to perpetrate any fraud on the stockholders. They were dealing with a person who held a majority of the stock and who in virtue thereof had the right and the power to control the corporation. . . . He had the right to sell out all his stock and interest in the corporation, and in doing so he perpetrated no wrong upon any one. . . . It is the general rule . . . that those who have the largest interest in corporations may control them. . . . When Brown and Seligman succeeded to the interest of the plaintiff, holding a majority of the stock . . . it was proper that they should have the control. . . . It

[the contract] was simply the mode of transferring the control of the corporation to those who by the policy of the law ought to have it, and I am unable to see how any policy of the law was violated or in what way, upon the evidence, any wrong was thereby done to any one." See, however, *contra*, *Fremont v. Stone*, 42 Barb. 169 (1864). But the directors have no power to contract with an outsider that he shall for a consideration be made a director in the company. *Seymour v. Detroit Copper, &c. Mills*, 56 Mich. 117 (1885).

¹ *Woodruff v. Wentworth*, 133 Mass. 309 (1882).

² Thus votes cannot be rejected because it appears that the stockholder offering them bought his stock for the purpose of obtaining control of the corporation: *Pender v. Lushington*, L. R. 6 Chan. Div. 70 (1877). The corporation cannot refuse to register transfers made merely to increase the voting capacity of the stock. *In re Stranton Iron & Steel Co.*, L. R. 16 Eq. 559 (1873). See also *People v. Kip*, 4 Cowen, 372, note (1822); *State v. Smith*, 48 Vt. 266 (1876).

³ *Griffith v. Jewett*, Cincinnati Superior Court, May, 1866, 15 Week. Law Bul. 419. Speaking of this trust agreement, the court, in an exceedingly able and luminous opinion, say: "The agreement may be finally reduced to this: The entire beneficial interest in the stock is severally vested in the certificate-holders, the voting power in the trustees, and

§ 619. *Failure to elect officers.*—A failure to elect officers at the stated time does not work a dissolution of the corporation. The old directors continue in office until their successors are duly elected.¹ And even when the failure to elect has extended over a period of several years and there are by reason thereof no directors in office, the old directors having wholly abandoned their trust, the stockholders may at any time in a lawful manner proceed to the election of a new board of directors.² But if the majority fail or refuse to hold an election and the corporate property is thereby endangered, a court of equity may appoint a receiver to take charge of it,³ and will, in a proper case, authorize a winding up.⁴

§ 620. *Who may be a director or corporate officer.*—In general any one who may be an agent may be elected a director of a private corporation, and at common law it is not necessary that a director be a stockholder,⁵ nor even a citizen of the State by which

the situation does not differ materially from what it would be if the stockholders retaining their shares had simply united in a proxy authorizing the trustees to cast the vote of all of them for directors. We can perceive no reason why any number of shareholders, either by means of a proxy or by vesting the legal title in another, may not authorize him to vote upon their stock, and as such is the substance of this agreement we consider it not illegal. So long as the parties to it, or their successors in interest, are satisfied with it, no other person may complain." In this case it was, however, held that this compact was not irrevocable though expressly declared to be so, and that at any time any shareholder who wished to do so might withdraw his stock and demand an ordinary certificate. In New York, where certain stockholders "for mutual protection and to prevent the sales of the company's franchise by a majority of the present board of directors, who are and who represent a minority of the shares of the capital stock," entered into a sealed agreement not to sell their stock nor to vote by proxy without the unanimous consent of all the parties to the contract, it was held that the agreement was void, as in restraint of trade and against public policy, and because an agreement not to vote by proxy was a pernicious

and unlawful provision. *Fisher v. Bush*, 35 Hun, 641 (1885).

¹ *State v. Bonnell*, 35 Ohio St. 10, 17 (1878); *Smith v. Silver Valley Mining Co.*, 64 Md. 85 (1885). See New York Laws of 1848, chap. 40, § 4.

² *People v. Twaddell*, 18 Hun, 427 (1879). In *Reilly v. Oglebay*, 25 West Va. 36, 43 (1884), it is held that where there is no board of directors the shareholders themselves may lawfully assume and perform, pending a regular election, the duties which ordinarily belong to a board of directors. See here in *Smith v. Silver Valley Mining Co.*, 64 Md. 85 (1885); s. c. 10 Am. & Eng. Corp. Cas. 1.

³ *Lawrence v. Greenwich Fire Ins. Co.*, 1 Paige, 587 (1829).

⁴ *Brown v. Union Ins. Co.*, 3 La. Ann. 177, 182 (1848); *Curry v. Woodward*, 53 Ala. 375 (1875); *Knowlton v. Ackley*, 8 Cush. 93 (1851). See *Bruce v. Platt*, 80 N. Y. 379 (1880).

⁵ *State v. McDaniel*, 22 Ohio St. 354, 367 (1872); *Wight v. Springfield, &c. R. Co.*, 117 Mass. 226 (1875); in the *Matter of Election of St. Lawrence Steamboat Co.*, 44 N. J. Law, 629 (1882); *Ex parte Stock*, 33 L. J. Chan. 731 (1864). Cf. *Dispatch Line of Packets v. Bellamy Manfg. Co.* 12 N. H. 205 (1841); *Bartholomew v. Bentley*, 1 Ohio St. 37 (1852).

the corporation is created.¹ But in modern corporations having a capital stock it is now almost universally the rule that directors can be chosen only from the stockholders; that to be eligible to that office a stockholder must own a specified amount of stock; and that a majority at least of the board of directors must be citizens of the State or country in which the corporation exists.² The qualification of directors in respect of residence or citizenship and the ownership of stock is usually determined, in the absence of statutory regulation, by a charter provision. If not, the corporation may prescribe it by a by-law or special resolution.³ A married woman may, in New York, be a director in an incorporated company;⁴ so also may one who holds stock transferred to him in trust for the express purpose of qualifying him for the position;⁵ and where a person has the right to vote on stock as a stockholder, even though that right rest only upon a power of attorney, he is eligible to any corporate office to which any stockholder is eligible, and accordingly may be elected a director.⁶ The election of one not a shareholder or a director in a corporation in which it is required that the directors be owners of a certain amount of stock is valid, and such a person, upon acceptance of the directorship, is bound to take and pay for the required number of shares.⁷

¹ *Kerchner v. Gettys*, 18 S. C. 521 (1882).

² The provision of the New York Manufacturing Companies Act, upon this point, has been widely copied in the acts of many other States. It is there enacted, that "The stock, property, and concerns of such company shall be managed by not less than three or more than thirteen trustees, who shall respectively be stockholders in such company and citizens of the United States, and a majority of whom shall be citizens and residents of this State, who shall, except the first year, be annually elected by the stockholders," &c. New York Laws of 1848, chap. 40, § 3. In Pennsylvania it is enacted, that the president and a majority of the board of directors of every railroad corporation created by the laws of that State, must be and remain resident within the State during the time they hold their office. *Brightly's Purdon's Digest*, 1229, § 86, 1233, § 103.

³ *People v. Northern R. R. Co.*, 42 N. Y. 217 (1870); *Cammayer v. United Church*, 2 Sandf. Chan. 186 (1844). But where the articles of association do not require

that a director be a shareowner, but the directors themselves pass a resolution, which is never confirmed by the shareholders, that the qualification in future shall be the ownership of 250 shares of £1 value each, it was held that such resolution could not alter the constitution of the company, or render one who became a director subsequently liable for that amount of stock on the winding up. *In re British Provident Life, &c. Association*, L. R. 5 Chan. Div. 306 (1876). *Cf.* *Lord Cland Hamilton's Case*, L. R. 8 Chan. 548 (1873).

⁴ *People v. Webster*, 10 Wend. 554 (1833).

⁵ *Budd v. Monroe*, 18 Hun. 316 (1879). *Contra*, *Bartholemew v. Bentley*, 1 Ohio St. 37 (1852).

⁶ *State v. Ferris*, 42 Conn. 560 (1875).

⁷ *In re The Great Oceanic Telegraph Co.*, 41 L. J. Chan. 283 (1872); *Pearson's Case*, L. R. 5 Chan. Div. 336 (1877); *Hay's Case*, L. R. 10 Chan. 593, 604 (1875). *Cf.* *De Ruigne's Case*, L. R. 5 Chan. Div. 306, 322 (1877); *In re Englefield Colliery Co.*, L. R. 8 Chan. Div. 388 (1877); *In re Empire Assurance Co.*, L.

Where the qualification of one to act as director of a company consists in his being the proprietor of a certain number of shares, the qualification will not be lost by a pledge of the shares.¹ But an absolute sale of the stock at any time prior to the termination of the directorship immediately disqualifies the director who sells, and he can no longer act.² Where one accepts the office of director without owning the required number of shares of stock, and is in consequence under obligation to qualify himself by taking stock, he is not obliged to take the stock from the company, but may purchase or procure the shares as he is able, in the open market, or at private sale.³ The election of an unqualified person to a corporate office is merely voidable, and not void.⁴

B.—OTHER CORPORATE FUNCTIONS BELONGING TO THE STOCKHOLDERS AS DISTINGUISHED FROM THE DUTIES OF DIRECTORS.

§ 621. *The general method of transacting business.*—It is a general rule that in the transaction of the ordinary business of a corporation, no particular formalities are necessarily to be observed. The proceedings must be conducted in an orderly manner, in accordance with the general usage, and where the charter or by-laws prescribe a particular manner of conducting the business, in the manner so prescribed.⁵ Mere irregularities in the manner of conducting the business are immaterial if the sense of the meeting has been fairly expressed.⁶ And such irregularities

R. 6 Chan. 469 (1871); McKay's Case, 2 Chan. Div. 1 (1875). *Contra*, Marquis of Abercorn's Case, 4 De G., F. & J. 78 (1862). Where the articles of association require that the directors own 25 shares, as a qualification for their office, one who is elected and acts as director without taking any shares, is liable on the winding up for the qualification number of shares. Stephenson's Case, 45 L. J. Chan. 488 (1876). *Cf. In re* British and American Telegraph Co., L. R. 14 Eq. 316 (1872).

¹ Cumming v. Prescott, 2 Y. & C. Exch. 488 (1837).

² *Craw v. Easterly*, 54 N. Y. 679 (1873); *Easterly v. Barber*, 65 Id. 252 (1875).

³ *Brown's Case*, L. R. 9 Chan. 102 (1873); *Karuth's Case*, L. R. 20 Eq. 506

(1875). *Contra*, *Hayward's Case*, L. R. 13 Eq. 30 (1871); also *Fowler's Case*, L. R. 14 Eq. 316 (1872); and *cf. Hamley's Case*, L. R. 5 Chan. Div. 705 (1877); *Barber's Case*, Id. 963 (1877); *Forbes Case*, L. R. 8 Chan. 768 (1873); *Chapman's Case*, L. R. 2 Eq. 567 (1866); *Maitland's Case*, 3 Giff. 28 (1861).

⁴ *People v. Albany, &c. R. R. Co.*, 55 Barb. 344 (1869). *Cf. Craw v. Easterly*, 54 N. Y. 679 (1873); *Easterly v. Barber*, 65 Id. 252 (1875).

⁵ *Johnston v. Jones*, 23 N. J. Eq. 216 (1872); *People v. Albany, &c. R. R. Co.*, 55 Barb. 344 (1869); *State of Nevada v. Pettineli*, 10 Nev. 141 (1875); *Commonwealth v. Woelper*, 3 Serg. & R. 29 (1817).

⁶ *Philips v. Wickham*, 1 Paige, 590

or informalities, if they exist, are waived by the acquiescence of those members who have a right to complain. Accordingly, presence at the meeting and participation in the proceedings will be held to waive the irregularity. So also equally will a failure upon the part of those members not present to protest promptly, upon learning of the informality, be a waiver.¹ In the absence of proof to the contrary, the presumption of law is that a corporate meeting was duly called and convened, and that the proceedings were lawful and regular.² When the irregularity or informality affects a substantial right of the stockholder, or amounts to fraud, he may have his action to set aside what has been done to his prejudice.³

§ 622. *Stockholders can act only at corporate meetings.*—

Stockholders can lawfully act in their corporate capacity only at a corporate meeting, duly called and convened. They cannot bind either themselves or the corporation in any other way than by a vote at such a meeting. Consequently, all votes taken elsewhere than at such a meeting, and all separate consents, either oral or in writing, whereby the stockholders assume to bind themselves or the company, are invalid and void.⁴

(1829); *Downing v. Potts*, 23 N. J. Law, 66 (1851); *People v. Albany, &c. R. R. Co.*, 55 Barb. 344 (1869); *Matter of Wheeler*, 2 Abb. Pr. (N. S.) 361 (1866); *Gorham v. Campbell*, 2 Cal. 135 (1852); *Hughes v. Parker*, 20 N. H. 58 (1849); *Hardenburgh v. Farmers, &c. Bank*, 3 N. J. Eq. 68 (1834); *People v. Peck*, 11 Wend. 604 (1834). In this case the irregularity complained of was want of due notice, but inasmuch as the meeting was generally attended, and the time of the meeting thoroughly understood, and no one complained at the time of want of notice, the court held the proceedings valid, saying: "The object of the notice is that the voters may be fully apprised of the election, and may attend and exercise their rights. There is no pretence in this case that every voter was not present, for they appear to have come from a distance; the time was well understood, and had been the same for many years. No evil resulted from the omission if there was any; no fraud was imputed, and all parties attended, and thereby admitted notice."

¹ *State v. Lehre*, 7 Rich. Law, 234, 325 (1854); *Prettyman v. Supervisors*, 19

Ill. 406 (1858); *The King v. Trevenen*, 2 Barn. & Ald. 339 (1819); *Musgrave v. Nevinston*, 2 Lord Raymond, 1358 (1737).

² *Blanchard v. Dow*, 32 Me. 557 (1851); *Ashtabula, &c. R. R. Co. v. Smith*, 15 Ohio St. 328 (1864).

³ See part IV, *infra*. Cf. *MacDougall v. Gardiner*, L. R. 1 Chan. Div. 13 (1875), where the extreme ground is taken that a stockholder cannot go into the courts and complain of irregularity in the proceedings of a corporate meeting, even though it materially affects his rights upon the theory, as it seems, that a court of equity will not interfere in the mere contests or disagreements of the members of a private corporation.

⁴ *Commonwealth v. Cullen*, 13 Penn. St. 133 (1850); *Finley Shoe, &c. Co. v. Kurtz*, 34 Mich. 89 (1876); *Peirce v. New Orleans Building Co.*, 9 La. 397, 404 (1836), where the court says: "We know of only two ways in which such a corporation as the one now under consideration can act, *to wit*: either through its president and directors, or at a meeting of the stockholders duly convoked. The act by which the defendants were incorporated does little more than give

§ 623. *Stockholders may make by-laws.*—One of the most important functions which shareholders perform in their corporate capacity, is the enactment of by-laws to regulate the corporation and the order of corporate meetings.¹ The power to make by-laws is a general power, subject only to the qualification that the by-laws must be reasonable, must not abridge the substantial rights of the stockholders, or be against public policy or the law of the land.²

the corporation a name, and a legal capacity. It provides for the appointment of directors, but is silent as to the manner in which the corporators are to be convoked, and how they are to vote, whether per capita or according to the amount of shares held by each. In these respects their proceedings, and the validity of their acts, must be judged of according to the principles of law applicable to corporations in general. If the two minority meetings be laid out of view as void, the whole rests upon the assent as expressed by a majority of the stockholders, not in a meeting of stockholders, but by each one separately and at different times, and evidenced, not by the minutes of their corporate proceedings, but by a separate paper in the possession of a committee. We cannot see in this any legal evidence of the consent of the corporation, either according to its charter or the general principles of law." *Cf. Graham v. Boston, Hartford & Erie R. R. Co.*, 118 U. S. 161 (1886); *Granger v. Grubb*, 7 Phila. 350 (1870).

¹ *People v. Crossley*, 69 Ill. 195 (1873); *Kearney v. Andrews*, 10 N. J. Eq. 70 (1854); *People v. Kip*, 4 Cowen, 382, note (1822); *Carroll v. Mullanphy Savings Bank*, 8 Mo. App. 249, 253 (1880); *Commonwealth v. Woelper*, 3 Serg. & R. 29 (1817); *Juker v. Commonwealth*, 20 Penn. St. 484 (1853); *Newling v. Francis*, 3 Term Rep. 189 (1789). *Cf. Samuel v. Hbladay*, 1 Woolw. 400 (1869).

² *Taylor v. Griswold*, 14 N. J. Law, 222 (1834); *Brewster v. Hartley*, 37 Cal. 15, 24 (1869); *Commonwealth v. Gill*, 3 Wharton, 228 (1837); *People v. Phillips*, 1 Denio, 388 (1845); *Rex v. Head*, 4 Burr. 2515 (1770). *Cf. Rex v. Spencer*, 3 Burr. 1827 (1766); *Petty v. Tooker*, 21 N. Y. 267 (1860), affirming s. c. *sub nom. Parish of Bellport v. Tooker*, 29 Barb. 256; *Burrel v. Associate Reformed Church*, 44 Barb. 282; *Watkins v. Wilcox*, 4 Hun, 220 (1875); s. c. affirmed, 66 N. Y. 654 (1876); *Graw v. Prussia Emigrated, &c. Society*, 36 N. Y. 160 (1867).

In the *Matter of the Long Island R. R. Co.*, 19 Wend. 37, 41 (1837), the court say: "The corporation possess the power to make by-laws not inconsistent with any existing law, for the management of its property, the regulation of its affairs, and for the transfer of stock (2 R. S. 602 § 1, sub. 6). This is the broadest general power conferred upon it; but it is not new, and would have existed as incidental. When taken as incidental it must be exercised in conformity to the general law of the land, that being the rule to regulate the proceedings of artificial bodies, as well as the conduct of natural persons, independently of express provisions of the charters of those companies to the contrary. This general law has ascertained the rights of person and of property of the citizen, and established modes of proceeding in case of a violation of them; and corporate bodies must conform to them, in seeking redress, the same as individuals. The former can no more take the remedy into their own hands than can the latter. So strict has this salutary principle of subjection been held in England, that even a by-law in pursuance of an express power in a charter granted by the King, is void, if contrary to the common law or Act of Parliament. (1 Kyd on Corp. 109; *Wilcox on Corp.* 95; *Angell & Ames*, 196; 8 Co. 125 a, 127 b; 2 Inst. 47; 1 T. R. 118). Thus, a by-law imposing a forfeiture of goods is void, though the letters patent authorized it; and a power granted to a corporation of dyers to search, and if they found cloth dyed with logwood, to seize it as forfeited, was adjudged void as contrary to magna charta. On the same principle, by-laws in restraint of trade are adjudged void. (11 Co. 53; 1 Burr. 12; 4 Id. 1951; 7 Dowd & Ryl. 601; 1 Bacon's Abr. 547; *Angell & Ames*, 184; *Willock*, 142). So a by-law that may be lawful cannot be enforced by an extraordinary penalty, such as imprisonment or forfeiture of goods, or by distress and sale of goods, for, by the general law of

When illegal by-laws which materially affect the rights of any shareholder, are enacted, the shareholder is not without a remedy. He may, in a proper case, and in a prescribed manner, assert his right in the courts.

§ 624. *The quorum.*—The right of the majority to rule in the management of the affairs of a private corporation, is fully established.¹ They may control the company's business, prescribe its general policy, make themselves its agents, and take reasonable compensation for their services.² The minority have a right to be heard, and it is the duty of the majority to give a due consideration to their arguments and wishes concerning the management of the corporate business.³ It is generally necessary, in order to the valid transaction of the corporate business, that a quorum of the stockholders be present, in person or by proxy, at the meeting, and, in the absence of evidence to the contrary, it will be presumed, when the validity of the acts of a corporate meeting is the issue, that a quorum was present.⁴ One person cannot constitute a quorum. It takes at least two members to make a corporate meeting,⁵ and where one person owns a majority of the stock,⁶ or all of it,⁷ or all but two shares,⁸ he does not in consequence thereof acquire the right to act for the corporation, or as the corporation, independently of the directors. But, in the absence of an express provision to the contrary, a majority in interest of the stockholders constitutes a lawful quorum for the

the kingdom, no man is to be imprisoned, or dispossessed of his goods and chattels *nisi per legale iudicium parium suorum, vel per legem terræ*; and if such penalties were allowed, corporations would be enabled to set up private particular laws in contradiction to the laws of the land, which is against the nature and essence of a by-law. (Clark's Case, 5 Co. 64; 3 Salk. 76; Willcock, 98; 1 Bacon's Abr. 551.)"

¹ City of Covington v. Covington, &c. Bridge Co., 10 Bush, 69, 76 (1873); East Tennessee, &c. R. R. Co. v. Gammon, 5 Sneed (Tenn.), 567 (1859); McBride v. Porter, 17 Iowa, 203 (1864); Faulds v. Yates, 57 Ill. 416 (1870); Leo v. Union Pacific R. R. Co., 19 Fed. Rep. 283 (1884); s. c. 17 Id. 273 (1883); Barnes v. Brown, 80 N. Y. 527 (1880).

² Meeker v. Winthrop Iron Co., 17 Fed. Rep. 48 (1883); s. c. *sub nom.* Winthrop Iron Co. v. Meeker, 109 U. S. 180 (1883).

³ Natusch v. Irving, 2 Cooper's Chan. 358 (1824), by Lord Eldon; Const v. Harrie, Turn. & R. 496 (1824). See also Blisset v. Daniel, 10 Hare, 493 (1853); Wood v. Woad, L. R. 9 Exch. 190 (1874).

⁴ Citizens' Mutual, &c. Ins. Co. v. Sortwell, 8 Allen, 217 (1864).

⁵ Sharpe v. Dawes, 46 L. J. (Q. B.) 104 (1876). The rule of course is otherwise if there is but one stockholder.

⁶ Hopkins v. Roseclare Lead Co., 72 Ill. 373 (1874). He cannot sell the corporate property.

⁷ Button v. Hoffman, 61 Wis. 20 (1884), where it is held that such a stockholder is not the corporation. *Contra*, Swift v. Smith, 6 East. Rep. 574; s. c. 3 Cent. Rep. 899 (Md. 1886); 34 Alb. Law Jour. 257.

⁸ England v. Dearborn, 141 Mass. 590 (1886). Such a stockholder cannot mortgage the corporate property.

transaction of business, and a majority of the quorum, although a minority of the whole number of stockholders, may decide any question, and bind the corporation upon any matter upon which the shareholders may lawfully act.¹ At a meeting duly convened, those shareholders who own a majority of the stock have power to transact business, although they are a minority of the whole number of shareholders.²

§ 625. *Stockholders, as such, cannot contract for the corporation.*—A corporation can act only through individual agents, who are the corporate officers or other persons. The stockholders themselves, in their capacity as stockholders, have, in meeting assembled, no power to act as agents in the transaction of corporate business. They cannot, by a direct vote, enter into contracts which will bind the corporation. It is held, under the operation of this rule, that the corporation cannot authorize outside parties, or even stockholders, to make a specific contract for the corporation. The management of the corporate affairs is intrusted to the directors. They are the constituted agents of the corporation, and to their judgment and discretion must be left the control and direction of the company's business.³ Ac-

¹ *Sargent v. Webster*, 13 Metc. 497 (1847); *Ex parte Willcocks*, 7 Cowen, 402 (1827); *People v. Walker*, 2 Abb. Pr. 421 (1856); s. c. 23 Barb. 308; *Field v. Field*, 9 Wend. 394 (1832); *Madison Ave., &c. Church v. Baptist Church*, 5 Robert. (N. Y. Super. Ct.) 649 (1867); *Everett v. Smith*, 22 Minn. 53 (1875); *Gifford v. New Jersey R. R. Co.*, 10 N. J. Eq. 171 (1854); *Dudley v. Kentucky High School*, 9 Bush, 578; *Durfee v. Old Colony, &c. R. R. Co.*, 5 Allen, 230, 242 (1862); *New Orleans, &c. R. R. Co. v. Harris*, 27 Miss. 517, 537 (1854); *Brown v. Pacific Mail Steamship Co.*, 5 Blatchf. 525 (1867); *Case of St. Mary's Church*, 7 Serg. & R. 517 (1822); *Craig v. First Presbyterian Church*, 88 Penn. St. 42 (1878). *Cf.* *Treadwell v. Salisbury Manfg. Co.*, 7 Gray, 393 (1856); *Stevens v. Rutland, &c. R. R. Co.*, 29 Vt. 545 (1851); *Stevens v. South Devon Ry. Co.*, 9 Hare, 313 (1851).

² *Granger v. Grubb*, 7 Phila. 350 (1870). Upon the question of the force and effect of acts done by less than a quorum, see *People v. Cook*, 14 Barb. 259, 315 (1852); *People v. Albany, &c. R. R. Co.*, 55 Id. 344, 385 (1869); s. c. 7 Abb. Prac. (N. S.) 265, 305; 1 Lans. 344.

³ *Conro v. Port Henry Iron Co.*, 12 Barb. 27 (1851); *McCullough v. Moss*, 5 Denio, 567 (1846); *Railway Co. v. Allerton*, 18 Wall. 233 (1873); *Union Gold Mining Co. v. Rocky Mountain Nat. Bank*, 2 Col. 565 (1875); *Methodist Episcopal Church v. Sherman*, 36 Wis. 404 (1874); *Salem Bank v. Gloucester Bank*, 17 Mass. 1, 29 (1820); *State of Louisiana v. Bank of Louisiana*, 6 La. 745 (1834); *Bank of Kentucky v. Schuylkill Bank*, 1 Parsons Sel. Cas. 180, 235 (1846). *Cf.* *People v. Metropolitan Ry. Co.*, 26 Hun, 32 (1881); *Howland v. Myer*, 2 Sandf. Super. Ct. 186; affirmed 3 N. Y. 290 (1850). *State of Nevada v. Curtis*, 9 Nev. 325 (1874); *Union Mutual, &c. Ins. Co. v. Keyser*, 32 N. H. 313 (1855); *Black v. Delaware, &c. Co.*, 22 N. J. Eq. 130 (1871); *Matter of Wheeler*, 2 Abb. Pr. (N. S.) 361 (1866); *Gashwiler v. Willis*, 33 Cal. 11 (1867); *Twin Lick Oil Co. v. Marbury*, 91 U. S. 587, 589 (1875); *Park v. Grant Locomotive Works*, 40 N. J. Eq. 114 (1885). See also *Fleckner v. United States Bank*, 8 Wheaton, 338 (1823); *Whitwell v. Warner*, 20 Vt. 425 (1848); *Ridgway v. Farmers' Bank*, 12 Serg. & R. 256 (1824). In *Metropolitan Elevated Ry. Co. v. Manhattan Ry. Co.* (New York

cordingly, a single stockholder cannot make a contract for and in the name of the corporation which shall have any binding force or validity, except by subsequent ratification or adoption in the regular manner.¹

In general the only powers vested in the stockholders, in respect of the management of the corporate enterprise, are the election of directors, the increase or reduction of the capital stock, the power of dissolving the corporation, of transferring the whole of the corporate property, and a few others of minor importance.²

C. P. April, 1884), 11 Daly, 377; s.c. 15 Am. & Eng. Ry. Cas. 1, Van Brunt, J., says: "Directors, as I shall hereafter attempt to establish, are the agents of the corporation, having, as such, exclusive authority to act within their sphere. But they are also in some respects, merely the executive agents of the stockholders, and as such may perform certain other acts, if specially authorized thereto by their principals, and in respect to such action they are simply the agents of the shareholders, as well as of the corporation. The shareholders, the principals, having fixed the terms and conditions, which they had a right to do, upon which the directors, their agents, were authorized to part with the possession of the property in their charge, and to commit the possession and management thereof into other hands; what right have the agents to radically change or alter these terms and conditions without consulting their principals. . . . The directors thus being the agents of the corporation, what are their powers, and from whence are they derived, and how must corporative powers residing in the corporation, the right to exercise which is not vested in the directors, be brought into operation? These questions are so intimately connected that, they must be disposed of together. The powers of directors are such as are conferred by the charter of their corporation and the laws pertaining thereto, and such corporative powers as are not conferred by law upon the directors, remain in the corporation to be exercised or at least set in motion by its component parts, the shareholders. In the case at bar, the charter provided that the directors were to manage the business and affairs of the company; and the question involved in this branch of the case is whether this language conferred the right to exercise every corporate power possessed by the corporation, or merely to

manage the ordinary business and affairs of the company for the carrying on of which it was organized, leaving the right remaining in the shareholders composing the company to set in motion or confirm corporate action within the limits of its powers, but extraordinary and unusual in its nature. Within the sphere of their duties, the right of the directors to act, is undoubtedly exclusive, and further, all corporate acts must be done through them, as they are the exclusive executive and administrative authority, but nevertheless all corporate powers do not reside in the board of directors."

¹ Robinson v. Hemstreet, 21 Fla. 342 (1885); Morelock v. Westminster Water Co. (Md. 1886), 4 Atlantic Rep. 404. Cf. Leggett v. New Jersey Manfg. & Banking Co., 1 Saxton's Chan. (N. J.) 541 (1832); s. c. 23 Am. Dec. 728 and the note. See also Rice v. Peninsular Club, 52 Mich. 87 (1883).

² Eidman v. Bowman, 58 Ill. 444 (1871), where the court says: "That the directors are but the agents or trustees of the shareholders, for the honest, faithful, and prudent management of the legitimate affairs of the shareholders, there is no doubt. But the question is as to the extent of their powers. Are they unlimited? Are all of the powers conferred on the company delegated to them by their election and admission to their office, or are there powers which are still reserved to the shareholders, and which cannot be exercised by them until the power is conferred by the shareholders? It would seem that the management and transaction of all business for which the company was created, and the general affairs of the corporation, devolved upon and may clearly be exercised by them; and there are other powers that are as clearly reserved to the shareholders. The power to appoint or elect directors does not devolve upon them, but that power is

Thus for example the directors of a corporation cannot lease the corporate property, or modify important covenants in an existing lease, except with the assent of the stockholders. Such transactions are for the stockholders to approve or disapprove at corporate meetings.¹ It is not, however, within the power of the stockholders to dictate to the directors how to act. Accordingly, where the stockholders at a corporate meeting give, by a formal vote, specific directions to the board of directors upon a matter which is within the proper scope of the discretion of the board, the directors are not bound to act in accordance with the directions so prescribed, nor will any court compel them to act in accordance with such dictation, even when a majority of the stockholders appeal for relief.² There is some authority for the proposition

reserved to the shareholders. The power to sell and transfer the charter and franchises is not granted to them; the power to dissolve the body is not within the scope of their authority; and other power which they are unable to exercise might be enumerated. Is the power possessed by them to effect great or radical changes in the organization of the body without the consent of the shareholders? Can they at pleasure and without the consent of the shareholders increase or diminish the capital stock of the company, and thus materially affect the value of the shares and the amount of dividends." See also *Hoyt v. Thompson*, 19 N. Y. 207 (1859).

¹ This is conclusively established in the case of the Metropolitan Elevated Ry. Co. v. Manhattan Ry. Co. (N. Y. C. P., April, 1884), *Van Brunt, J.*, 15 Am. & Eng. Ry. Cas. 1. See *Cass v. Manchester*, 13 Rep. 167; *Flagg v. Metropolitan Railway Co.*, 20 Blatchf. 142; *Martin v. Continental Pass. Ry. Co.*, 14 Phila. 10; *Woodruff v. Erie R. R. Co.*, 93 N. Y. 609 (1883); *Abbott v. Johnstown, &c. R. R. Co.*, 80 Id. 27; *People v. Albany, &c. R. R. Co.*, 77 Id. 232; *Troy, &c. R. R. Co. v. Boston, &c. R. R. Co.*, 86 Id. 107. Cf. *In the Matter of St. Ann's Church*, 23 How. Prac. 285; *Robertson v. Bullions*, 11 N. Y. 243 (1854); *Elwell v. Dodge*, 33 Barb. 339; *Matter of Excelsior Fire Ins. Co.*, 19 Abb. Prac. 14; *Dana v. Bank of the United States*, 5 Watts & S. 246; *Fisher v. New York, &c. R. R. Co.*, 46 N. Y. 644; *Central Crosstown Co. v. Twenty-third St., &c. Co.*, 54 How. Prac. 183; *Duncomb v. New*

York, &c. R. R. Co., 84 N. Y. 190 (1881); *Jackson v. New York, &c. R. R. Co.*, 58 N. Y. 623 (1874).

² *Conro v. Port Henry Iron Co.*, 12 Barb. 27 (1851); *McCullough v. Moss*, 5 Denio, 567 (1846); *Hoyt v. Thompson*, 19 N. Y. 207 (1859); *Dispatch Line of Packets v. Bellamy Manfg. Co.*, 12 N. H. 205, 226 (1841); *Salem Bank v. Gloucester Bank*, 17 Mass. 1, 29 (1820); *State of Louisiana v. Bank of Louisiana*, 6 La. 746; *Commonwealth v. Trustees of St. Mary's Church*, 6 Serg. & R. 508 (1821); *Dana v. Bank of the United States*, 5 Watts & S. 223, 245 (1843); *Dayton, &c. R. R. Co. v. Hatch*, 1 Disney, 84 (1855); *Union Gold Mining Co. v. Rocky Mountain Nat. Bank*, 2 Col. 565 (1875); *Union Mut. Fire Ins. Co. v. Keyser*, 32 N. H. 313. The directors can lawfully act only when duly convened as a board. *Gashwiler v. Willis*, 33 Cal. 11 (1867). Cf. *Granger v. Grubb*, 7 Phila. 350 (1870), where it was held that a vote ordered by the directors to be taken by a circular addressed to the stockholders, is not binding, but merely advisory. In *Bank of the United States v. Dandridge*, 12 Wheaton, 64, 113 (1827), it is said: "The directors are elected by the stockholders, and manage all their affairs, in virtue of the power conferred by the election. The stockholders impart no authority to them, except by electing them as directors. But, we are told, and are told truly, that the authority is given in the charter. The charter authorizes the directors to manage all the business of the corporation. But do they act as individuals, or in a corporate character? I

that when the legislature gives the corporation the privilege of altering or amending the charter the board of directors are entitled to act in making the changes, but the better rule is that the power to accept an amendment of the charter belongs to the stockholders and can be exercised only by them in corporate meeting assembled.¹

they act as a corporate body then the whole law applies to them as to other corporate bodies. If they act as individuals then we have a corporation which never acts in its corporate character, except in the instances of electing its directors or instructing them. The corporation possesses many important powers and is as a corporation to perform many important acts, scarcely one of which is to be performed in a corporate character. They are all to be performed by agents, acting as individuals under general powers conferred by the charter." So also, in *Forbes v. Memphis, &c. R. R. Co.*, 2 Woods, 331 (1872), the court thus define the rights and powers of the shareholders: "A commercial or other business corporation is constituted for the specific purpose of suing and being sued, granting and receiving, buying and selling, and doing other business in a corporate name and capacity totally distinct from that of any or all of its members considered as individuals. A corporation is a person. Its property is not the property of its stockholders. Its rights are not their rights. They have only an indirect interest therein. The rights of a stockholder are to meet at stockholders' meetings, to participate in the profits of the business, and to require that the corporate property and funds shall not be diverted from their original purpose. If the company become insolvent it is the right of the stockholders to have the property applied to the payment of its debts. I do not know of any other rights, except incidental ones, subsidiary or auxiliary to these. Of course a stockholder has ordinarily a right to a certificate for his stock, to transfer it on the company's books, and to inspect these books. For the invasion of these rights by the officers of the company he may sue at law or in equity, according to the nature of the case." The shareholders cannot maintain or defend suits for the corporation. *Blackman v. Central R. R., &c. Co. of Ga.*, 58 Ga. 189 (1877); *Silk Manfg. Co. v. Campbell*, 27 N. J. Law, 539 (1859). But a minority or even a single

stockholder may, in a proper case, sue the corporation for fraud. *Peabody v. Flint*, 6 Allen, 52, 55 (1863); *Allen v. Curtis*, 26 Conn. 456, 461 (1857). See Part IV, *infra*.

¹ In *Railway Company v. Allerton*, 18 Wall. 233, 235 (1873), Bradley, J., says: "As it respects the constituency or capital and membership, this is the next most important and fundamental point in the constitution of a body corporate. To change it without the consent of the stockholders would be to make them members of an association in which they never consented to become such. It would change the relative influence, control, and profit of each member. If the directors alone could do it, they could always perpetuate their own power. Their agency does not extend to such an act, unless so expressed in the charter, or subsequent enabling act; and such subsequent act, as before said, would not bind the stockholders without their acceptance of it, or assent to it in some form. Even when the additional stock is distributed to each stockholder *pro rata*, it would often work injustice, because many of the stockholders might be unable to take their respective share, and might thus lose their relative interest and influence in the corporate concerns." See also *Marlborough Manfg. Co. v. Smith*, 2 Conn. 579, 583 (1818), where the court said: "The directors had the management of the concerns of the company; but this did not enable them to apply to the legislature for an increase of their powers. Such application could be made by the authority of the company only. The resolve of the Assembly giving power to the company to assess the stockholders was void, because the application was made by the directors only, without any authority from the company. But if the power had been given to the company it could only have been exercised by the stockholders at a proper meeting. As the assessment in question was made by the directors, without any authority from the company, it is void." See §§ 496-500, *supra*.

§ 626. *The expulsion of members.*—In joint-stock companies, or in any corporation owning property, no power of expulsion can be exercised unless expressly conferred by the charter or by statute.¹ The expulsion by virtue of a by-law has been held to be unlawful.² A member who has been unjustly expelled may have *mandamus* to compel the corporation to restore him to membership.³ Accordingly, where a corporate body strikes off the name of one of its members without giving him previous notice of their intention so to do, and affording him opportunity to be heard in his own defense, a *mandamus* to restore will be granted,⁴ and an injunction lies to restrain a board of brokers from irregularly expelling one of their members,⁵ but not as against a medical society.⁶ So also the courts will not grant an injunction to restrain a corporation from initiating new members upon the application of a member of the corporation, when no danger of pecuniary loss is shown as likely to result to the petitioner from such initiation.⁷ Where the expulsion is regular and authorized by the charter or statute it is conclusive and *mandamus* will not lie.⁸ An act of expulsion cannot be impeached or attacked collaterally.⁹ At common law there were three causes for expulsion: where the member was guilty of an infamous, indictable of-

¹ *Evans v. Philadelphia Club*, 50 Penn. St. 107 (1865); *State v. Chamber of Commerce*, 20 Wis. 63 (1865); also *State v. Chamber of Commerce*, 47 Wis. 670 (1879). In *Dickinson v. Chamber of Commerce*, 29 Wis. 45 (1871), it is held that there may be a lawful expulsion under a valid by-law.

² *People v. Saint Francisco's Benevolent Society*, 24 How. Prac. 216 (1862); *Roehler v. Mechanics Aid Society*, 22 Mich. 86; *Green v. African Methodist Epis. Society*, 1 Serg. & R. 254. A resolution spread upon the corporate records unjustly expelling a member is a libel, and the member offering the resolution is liable to an action thereupon. *Fawcett v. Charles*, 13 Wend. 473 (1835). *Cf. Adley v. Whitstable Co.*, 19 Vesey, 304 (1815); *Chase v. East Tennessee, &c. Railroad Co.* 5 Lea (Tenn.), 415 (1880).

³ *Black & White Smith's Society, Vandyke*, 2 Wharton (Penn.), 309 (1836); *Commonwealth v. German Society*, 15 Penn. St. 251 (1850); *People v. Saint Francisco's Benevolent Society*, *supra*; *State v. Carteret Club*, 40 N. J. Law, 295; *People v. Medical Society of Erie Co.*, 32

N. Y. 187 (1865); *People v. New York Benevolent Soc.*, 3 Hun, 361 (1875); *Medical, &c. Society v. Weatherly*, 75 Ala. 248.

⁴ *Delacy v. Neuse River Navigation Co.*, 1 Hawks' Law (N. C.), 274 (1821). The member must have a fair hearing. *Southern Plank Road Co. v. Hixon*, 5 Ind. 165 (1854).

⁵ *Leech v. Harris*, 2 Brews. (Penn.) 571 (1870). *Cf. Society of Italian Union, &c. v. Montedonico* (Ky. 1884), 4 Am. & Eng. Corp. Cas. 22.

⁶ *Gregg v. Mass. Medical Society*, 111 Mass. 185 (1872).

⁷ *Thompson v. Society of Tammany*, 17 Hun, 305 (1879).

⁸ *Commonwealth v. Pike Beneficial Society*, 8 Watts & S. 247 (1844); *People v. Fire Underwriters*, 7 Hun, 248 (1876).

⁹ *Black & White Smith's Society v. Vandyke*, 2 Wharton (Penn.), 309 (1836); *Commonwealth v. Pike Beneficial Society*, 8 Watts & S. (Penn.) 247 (1844); *Society for the Visitation of the Sick v. Meyer*, 52 Penn. St. 125, 131 (1866). *Cf. Commonwealth v. Oliver*, 2 Parson Sel. Cases, 420, 426 (1849).

fense; or guilty of an offense against his duty as a corporator; or of an offense compounded of these two.¹

§ 627. *The removal of directors.*—The stockholders have in general no power to remove directors before the expiration of their term as fixed by charter or statute.² The corporators may, however, as of course, lawfully accept the resignation of such of the officers of the company as resign their offices.³ And where the stockholders have power by charter or statute to remove the directors for cause, the exercise of their discretion therein will not be reviewed in equity.⁴ So, likewise, where such a power is given to the stockholders, a court of chancery will not enjoin the

¹ James Bagg's Case, 11 Coke, 94, 99 (1616); *Rex v. Town of Liverpool*, 2 Burr. 723, 732 (1759); *State v. Chamber of Commerce*, 20 Wis. 63 (1865); *People v. New York Commercial Association*, 18 Abb. Prac. 271 (1864); *People v. Chicago Board of Trade*, 45 Ill. 112 (1867). *Cf. Smith v. Smith*, 3 Desauss. S. C. 557 (1813), where an expulsion for misconduct was sustained. *Woolsey v. Independent Order, &c.* (Iowa, 1883), 1 Am. & Eng. Corp. Cas. 172; *Fisher v. Keane*, L. R. 11 Chan. Div. 353; *Hopkinson v. Exeter*, L. R. 5 Eq. 63; *Dawkins v. Antrobus*, L. R. 17 Chan. Div. 615; *Gardner v. Freemantle*, 19 W. R. 256; *People v. New York Cotton Exchange*, 8 Hun, 216 (1876); *Dean v. Bennett*, L. R. 6 Chan. 489. In *Sturgis v. Board of Trade*, 86 Ill. 441 (1877), it was held that the remedy of the expelled member was at law and not in equity. But see *State v. Lusitanian Portuguese Society, &c.*, 15 La. Ann. 73 (1860); *Wood v. Wood*, L. R. 9 Exch. 190 (1874); *Bostwick v. Fire Department of Detroit*, 49 Mich. 513; *Hassler v. Phila. Musical Ass.*, 14 Phila. 233; *Anacosta Tribe v. Murbach*, 13 Md. 91; *State v. Georgia Medical Soc.* 38 Ga. 608; *Washington Benevolent Soc. v. Bacher*, 20 Penn. St. 425; *Riddell v. Harmony Fire, &c. Co.* 8 Phila. 310; *State v. Adams*, 44 Mo. 570; *Harmstead v. Washington Fire, &c. Co.*, 8 Phila. 381; *Commonwealth v. Philanthropic Soc.*, 5 Binn. 486; *Commonwealth v. St. Patrick Soc.*, 2 Id. 448; *People v. Fire Underwriters*, 14 N. Y. Super. Ct. 248. Upon the general question of the power to expel members see *Angell & Ames on Corp.*, § 410 *et seq.*; 2 Kent's Com. 297.

² *Imperial, &c. Hotel Co. v. Hampson*,

L. R. 23 Chan. Div. 1, 7 (1882). In this case the court, speaking to this point, say: "The only other question is whether the power is inherent in a corporation—it is quite plain to me it is not incidental to a corporation. As regards the corporators themselves it has been decided that in ordinary corporations there is a power of removal from the corporation for good cause. From the nature of the case one would assume that. . . . So in the same way you might make by-laws that whenever a corporator was incapable of exercising his functions, either from personal incapacity or because he had become infamous or otherwise unfit, he might be removed from the corporation; but all that is a necessary incident for carrying out the purposes for which the corporation is created, and it stands on a totally different footing from removing a person from an office in the corporation. It appears to me there is no doctrine of the common law, and there is no statutory provision which enables you to vary the contract entered into between the members, that the directors shall hold office for a given period, supposing there is a contract which does not contain the power of removal. That special power not being there, I think disposes of the notion that you can remove by some inherent power not contained in the statute or the articles." See also *Ex parte Paine*, 1 Hill, 665 (1841); *State of Ohio v. Bryce*, 7 Ohio (pt. 2d), 82 (1836); and for a contrary rule, *Burr v. McDonald*, 3 Gratt. 206 (1846); *Bayless v. Orme*, *Freeman's Ch. (Miss.)* 161 (1841).

³ *Cloutman v. Pike*, 7 N. H. 209 (1834).

⁴ *Inderwick v. Snell*, 2 Mac. & G. 216 (1850).

holding of a meeting called by the stockholders to consider, among other matters, the removal of the directors.¹ But where the officers depart from the line of their duty and are guilty of fraudulent, or negligent, or *ultra vires* acts, which the majority of the stockholders cannot or will not ratify, any one of the stockholders may appeal to the courts for relief. The officers themselves cannot, however, be removed by the corporation for such offenses.²

¹ Isle of Wight Ry. Co. v. Tabourdin, L. R. 25 Chan. Div. 320 (1883). For the provisions of the English statute in detail upon the question of the removal of di-

rectors by the corporation, see Stat. 8 & 9 Vict., chap. 16, §§ 70, 88, 89, 90, 91; Vol. IX, Rev. Stat., pp. 576 *et seq.*

² *Vide* Part IV, *infra*.

CHAPTER XXXVIII.

DISSOLUTION.

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| <p>§ 628. Methods of dissolution.</p> <p>629. Voluntary dissolution by unanimous consent.</p> <p>630. Whether a majority may dissolve.</p> <p>631, 632. Whether a minority may dissolve.</p> <p>633. What will and what will not operate to dissolve.</p> <p>634. Statutes regulating dissolution.</p> | <p>§ 635. The English statute.</p> <p>636. A lease or transfer of corporate property and franchises as a means of dissolution.</p> <p>637. Dissolution by legislative repeal of forfeitures, or by judicial forfeiture, or by lapse of time.</p> <p>638, 639. The assets upon dissolution.</p> |
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§ 628. *Methods of dissolution.*—The dissolution of a corporation may be brought about by reason of (1) the forfeiture of its franchises by the adjudication of a court; (2) the loss of its charter by a charter provision to that effect, in case the corporation fails to do certain things within a certain time¹; (3) the repeal of its charter under the reserved power of the State; (4) the voluntary surrender of the franchises by the corporation; or (5) the expiration of the time limited for its existence in the charter. Upon dissolution by any one of these methods, the stockholders have certain rights in the corporate assets. A consideration of the law governing dissolution by the first, second, third, and fifth methods is not within the scope of this treatise. This chapter is accordingly devoted to dissolution by a voluntary surrender of the franchises, and to the rights of stockholders in the corporate assets upon a dissolution of the corporation by any one of the five methods indicated.

§ 629. *Voluntary dissolution by unanimous consent.*—It is an unquestioned rule that all the stockholders, by unanimous consent, may effect a dissolution of the corporation by a surrender of the corporate franchises.² A railroad corporation stands

¹ See Brooklyn, &c., Co. v. City, 78 N. Y. 529; *In re* Brooklyn, &c., R. R. Co., 72 N. Y. 245; *Id.*, 75 N. Y. 335.

² Washington & Baltimore T. P. Road v. State, 19 Md. 239 (1862); Enfield Toll Bridge Co. v. Conn. River Co., 7 Conn. 28, 45 (1828); Mobile & Ohio R. R. Co. v. State, 29 Ala. 573, 586 (1857); Savage

v. Walshe, 26 Id. 619 (1855); Attorney-General v. Clergy Society, 10 Rich. Eq. 604 (1859); Chesapeake & Ohio Canal Co. v. Baltimore & Ohio R. R. Co., 4 Gill & J. 1, 121 (1832); McIntire Poor School v. Zanesville Canal, &c., Co., 9 Ohio, 203 (1839); Mummo v. Potomac Co., 8 Peters, 281, 287 (1834); La Grange

upon a somewhat different footing as respects its voluntary dissolution, and while such a corporation may undoubtedly abandon its charter and dissolve itself, yet inasmuch as it is a *quasi* public corporation, this right is limited or qualified as to the power to dispose of the eminent domain franchises which it is exercising. The legislature may, however, release it from this limitation, and transfer those duties to other persons or another corporation.¹ A voluntary dissolution may be effected by an express act of the stockholders.²

& *Memphis R. R. Co. v. Rainey*, 7 Coldw. (Tenn.) 420 (1870); *Slee v. Bloom*, 19 Johns. 456 (1822); *Webster v. Turner*, 12 Hun, 264 (1877). *Cf.* *The King v. Amery*, 2 Term Rep. 515, 531 (1788); *The King v. Gray*, 8 Modern Rep. 358, 361; *McLaren v. Pennington*, 1 Paige, 102, 107 (1828); *Riddle v. Merrimac Locks*, 7 Mass. 169, 185 (1810); *Hampshire v. Franklin*, 16 Id. 76, 87 (1819). In *Penobscot Boom Corp. v. Lamson*, 16 Me. 224 (1839), the court say: "It is contended also that if the corporation has existed it has been dissolved. In what manner corporations may be dissolved, and what will operate as a dissolution, has been determined in many decided cases. A corporation will not be dissolved by a sale of the franchise, or of all the corporate property and a settlement of all its concerns and a division of the surplus, or by a cessation of all corporate acts, or by any neglect of corporate duty, or any abuse of corporate powers, or by doing acts which cause a forfeiture of the charter without a judgment declaring such forfeiture. Such dissolution can take place only (1) by an act of the legislature, where, as in this State, power is reserved for that purpose; (2) by a surrender, which is accepted, of the charter; (3) by a loss of all its members, or of an integral part, so that the exercise of corporate functions cannot be restored, (4) by forfeiture, which must be declared by judgment of court." *s. p.* *Hodsdon v. Copeland*, 16 Me. 314 (1839). In *Houston v. Jefferson College*, 63 Penn. St. 428 (1869), it is said upon this point: "The general right of a private corporation to surrender its franchises may possibly have exceptions, but undoubtedly it is the rule. This is generally described as an inherent right, which would necessarily defeat any attempt by legislation to enforce upon a corporation qualities of perpetuity. Such a thing would be im-

possible in the nature of things. Corporations, like individuals, die by the decay or loss of their vital functions, and this effectually defies authority to render them perpetual. A surrender of a franchise is the voluntary death of the corporation, and is one mode by which it may cease to exist. 19 Johns. 478; 8 Pet. 381. If anybody ever did dispute the right of a corporation to surrender its franchise of its own mere motion, it is not likely that such a contest about the question could be long maintained where both parties, the State and the corporation, the grantor and grantee, consent to it, absolutely or on condition. This I take to be incapable of dispute, and the history of this college will show that this is just what has transpired in its case. It is undisputed in the pleadings." In *Graham v. Railroad Co.*, 102 U. S. 148 (1880), it was held that where a corporation, solvent at the time, and without intent to defraud creditors, disposed of its property for an inadequate consideration by a voluntary conveyance, its creditors cannot subsequently question the transaction.

¹ *Lauman v. Lebanon Valley R. R. Co.*, 30 Penn. St. 42 (1858). *Cf.* *Portland Dry Dock, &c., Co. v. Trustees of Portland*, 12 B. Mon. 77 (1851).

² Thus, where it was unanimously agreed at a stockholders' meeting—all the corporators being present in person, or by proxy—to sell all the corporate property, to cease to do business, and to consider the corporation dissolved, it was held, in a suit by one of the stockholders to compel the directors to call meetings and continue the business, that the acts of the corporation constituted a surrender of its corporate rights, and that it no longer existed. *Webster v. Turner*, 12 Hun, 264 (1877). *Cf.* *Abbot v. American Hard Rubber Co.*, 33 Barb. 578 (1861), upon the right of a proxy to vote for dissolution. A voluntary dissolution

It is not entirely settled whether an acceptance by the State of the surrender of the corporate franchise is necessary to complete the dissolution. It is, however, a general rule that there must be an acceptance, either by the legislature by which the franchise was conferred or by a court of competent jurisdiction as representing the State, in order that the surrender may operate fully to dissolve the corporation.¹ A decree of court is the more

is generally brought about by formal action by the stockholders. In such cases the officers are the proper parties to act for the corporation. *Bank of Switzerland v. Bank of Turkey*, 5 L. T. (N. S.) 549 (1862); *Treadwell v. Salisbury Manfg. Co.*, 7 Gray, 393 (1856); *In re Suburban Hotel Co.*, L. R. 2 Chan. 737 (1867); *Re Factage Parisien*, 34 L. J. Chan. 140 (1865); s. c., 13 W. R. 214, 330; *Marr v. Union Bank*, 4 Coldw. (Tenn.) 484; *Hancock v. Holbrook*, 9 Fed. Rep. 353 (1881). In general, however, the directors of a corporation are its agents to manage its affairs and carry out the purpose and object of its formation, and not to inflict upon it political death. They cannot, therefore, move for the dissolution of the company without express authority from the stockholders. *Abbot v. American Hard Rubber Co.*, 33 Barb. 578 (1861); *Buford v. Keokuk Northern, &c., Packet Co.*, 3 Mo. App. 159 (1876). A corporation cannot sell or assign its franchise, either in whole or in part, unless specially authorized by law. *Wood v. Bedford & Bridgeport R. R. Co.*, 8 Phila. 94 (1871) (by Sharswood, J.). *Cf. Graham v. Railroad Co.*, 102 U. S. 148 (1880). As to a forfeiture for a non-user of the corporate franchises, in New York, it is provided by statute (1 New York Rev. Statute, 604, § 4; 2 Id. 463, § 38), that a corporation shall be deemed or adjudged to be dissolved when it shall have remained insolvent, or neglected, or refused to pay its notes, or evidences of debt, or suspended its business for one year. See, for the construction of these statutes, *Denike v. New York, &c., Cement Co.*, 80 N. Y. 599 (1880), where it is held that a corporation cannot be said, under these statutes, to have committed an act of insolvency, or to have neglected or refused to pay its obligations, because its demand notes remain outstanding until payment has been demanded. In *Brandt v. Benedict*, 17 N. Y. 93 (1858), these statutes are held to be cumulative, and not a limi-

tation upon the common law rule previously existing in New York. Accordingly, in order to infer a surrender of corporate franchises from insolvency and suspension of business for less than a year, the circumstances must be such as to show that the corporation has lost all power to continue or resume its business. So in Tennessee, at common law, it is held that if a private corporation suffer all their property to be sacrificed, and the corporate management relinquishes the trust, omits the annual election, and does no act manifesting an intention to resume the corporate functions, the courts will, in favor of creditors, presume a virtual surrender of the corporate rights and a dissolution of the corporation. *La Grange & Memphis R. R. Co. v. Rainey*, 7 Coldw. (Tenn.) 420, 438 (1870).

¹ *Portland Dry Dock, &c., Co. v. Trustees of Portland*, 12 B. Mon. 77 (1851); *La Grange & Memphis R. R. Co. v. Rainey*, 7 Coldw. (Tenn.) 420 (1870); *Polar Star Lodge v. Polar Star Lodge*, 16 La. Ann. 53 (1861); *Currien v. Santini*, Id. 27 (1861); *Campbell v. Miss. Union Bank*, 7 Miss. 625, 681 (1842); *Norris v. Mayor of Smithville*, 1 Swan (Tenn.), 164 (1851); *Mechanics Bank v. Heard*, 37 Ga. 401 (1867); *Boston Glass Co. v. Langdon*, 24 Pick. 49 (1834); *Wilson v. Proprietors of Central Bridge*, 9 R. I. 590 (1870); *Penobscot Boom Corp. v. Lamson*, 16 Me. 224 (1839); *Enfield Toll Bridge Co. v. Conn. River Co.*, 7 Conn. 28, 45 (1828); *Ward v. Sea Ins. Co.*, 7 Paige, 294 (1838); *New York Marbled Iron Works v. Smith*, 4 Duer, 362 (1855). *Cf. Nimmons v. Tappan*, 2 Sweeney (N. Y. Super. Ct.), 652 (1870); *Revere v. Boston Copper Co.*, 15 Pick. 351 (1834). In *Harris v. Muskingum Manfg. Co.*, 4 Blackf. (Ind.) 267 (1836), where a corporation being sued on a debt plead a voluntary dissolution, the court said: "To say, merely, as this plea does, that the corporation had been dissolved by the consent and act of its members, is not sufficient. A corporation cannot be

usual manner in which such a surrender is accepted.¹ But some of the older cases intimate that the acceptance of such a surrender should be by the legislature, presumably upon the theory that the surrender should be directly to the legislature, because the franchise was granted by that body, and because it alone can properly receive or accept back a relinquishment of the franchises and privileges which it confers.² But the practical difficulty, in modern times, of procuring the passage of a special act for this purpose, for every dissolution, is sufficient to prevent such a rule from obtaining general sanction. Many States have statutes authorizing the courts to accept a voluntary surrender of cor-

dissolved by the consent of its members, except it be by the surrender of their franchise to the government, and an acceptance by the government of the surrender. But this plea shows no such surrender and acceptance, and is consequently bad." In *Town v. Bank of River Raisin*, 2 Doug. (Mich.) 530 (1847), the court says: "No rule is better settled than that a corporation may be dissolved by the surrender of its franchises of being a corporation into the hands of the government. . . . The modes in which a surrender is to be made, and as to what facts constitute a surrender, have been a fruitful subject of discussion in the courts of this country. In England the surrender is by deed to the King, by whom corporations are usually created by charter. In this country, corporations are created by an act of the legislature, and it would seem to follow, in the absence of any statute prescribing the mode in which a surrender is to be made, that to become available, it must be accepted by the authority which created the corporation. I have no doubt that a surrender made by the great body of the society, and accepted by the legislature, would operate as a dissolution of the corporation; but such a surrender and acceptance would not perhaps, in this country, absolve the corporation from any of its liabilities. . . . Regarding an act of incorporation, when accepted, as a contract between the State and the corporation, it would then appear necessary, in order to dissolve a corporation, that the consent of both parties should be obtained. If, therefore, the members of a corporation are desirous of bringing its business to a close, a resolution to surrender by the great body of the corporators, being presented to the

legislature, and assented to by that body in the form of a legislative act, would be effectual to dissolve the corporation. So an act of the legislature repealing the charter, if assented to by the corporation, would operate as a dissolution. That a corporation, by its own act, can dissolve itself, is no where asserted, nor can it be sustained; this must be done by the concurrence of the parties to the compact, or by the solemn judgment of a court of competent jurisdiction." No cause of forfeiture, however, can be taken advantage of collaterally. *Chesapeake & Ohio Canal Co. v. Baltimore & Ohio R. R. Co.*, 4 Gill & J. 1, 107 (1832).

¹ *Boston Glass Co. v. Langdon*, 24 Pick. 49, 53 (1834); *Town v. Bank of River Raisin*, 2 Doug. (Mich.) 530, 539 (1847); *La Grange & Memphis R. R. Co. v. Rainey*, 7 Coldw. (Tenn.) 420, 438 (1870); *Revere v. Boston Copper Co.*, 15 Pick. 351 (1834); *Mechanics Bank v. Heard*, 37 Ga. 401 (1867); *Wilson v. Proprietors of Central Bridge*, 9 R. I. 590 (1870); *Norris v. Mayor of Smithville*, 1 Swan (Tenn.), 164 (1851); *Eusfield Toll Bridge Co. v. Conn. River Co.*, 7 Conn. 28, 45 (1828); *West v. Carolina Life Ins. Co.*, 31 Ark. 476 (1876).

² Accordingly, in England the surrender at common law was to the King, and must be accepted by him in order to work a dissolution. *The King v. Amery*, 2 Term Rep. 515, 531 (1788); *The King v. Gray*, 8 Mod. Rep. 358 (1825). See *Town v. Bank of River Raisin*, 2 Doug. (Mich.) 530, 538 (1847), where the court says: "I have no doubt that a surrender made by the great body of the society, and accepted by the legislature, would operate as a dissolution of the corporation."

porate franchises, and it is probable that the courts of those States which have no such statute, would take the ground that they possessed a common law power in a proper case to accept such a surrender.

§ 630. *Whether a majority may dissolve.*—A difficult question, as to the power to work a dissolution, arises when those stockholders who own a majority of the stock wish to dissolve the corporation, while the remaining minority of the stockholders oppose it. The courts are not entirely agreed, but it is the more general rule that while a majority of the stockholders cannot, in opposition to the wishes of even a single stockholder, work any radical change in the nature and character of a going concern, such a majority may, if they elect, dissolve the corporation by a surrender of the franchises.¹ It has been held, however, when the duration of the corporation is fixed by the charter, that a minority may prevent a dissolution.² So also there is some

¹ *Bank of Switzerland v. Bank of Turkey*, 5 L. T. (N. S.) 549 (1862); *Treadwell v. Salisbury Manfg. Co.*, 7 Gray, 393 (1856); *Hancock v. Holbrook*, 9 Fed. Rep. 353 (1881); *Wilson v. Proprietors of Central Bridge*, 9 R. I. 590 (1870); *Lauman v. Lebanon Valley R. R. Co.*, 30 Penn. St. 42 (1858); *McCurdy v. Myers*, 44 Id. 535 (1863); *Revere v. Boston Copper Co.*, 15 Pick. 351 (1834); *Black v. Delaware, &c., Canal Co.*, 22 N. J. Eq. 130, 192, 404 (1871); *Zabriskie v. Hackensack, &c., R. R. Co.*, 18 Id. 193 (1867). *Cf. Kean v. Johnson*, 9 N. J. Eq. 401 (1853); *Mobile & Ohio R. R. Co. v. State*, 29 Ala. 573 (1857); *Wilson v. Miers*, 10 C. B. (N. S.) 348 (1861). *Contra, Curien v. Santini*, 16 La. Ann. 27 (1861); *Polar Star Lodge v. Polar Star Lodge*, Id. 53 (1861). In *Ward v. Society of Attornies*, 1 Coll. 370 (1844), Bruce, V. C., granted an injunction on a motion made on behalf of a minority, to restrain the majority of the members of an incorporated society of attornies, until the minority could be heard, from surrendering their charter, with a view to obtain a new charter for a different object. A court is not bound to decree a dissolution of a corporation merely because a majority of the directors and stockholders apply for a repeal of the charter, and desire the dissolution. But where the owners of a large proportion of the stock find it for their interest to withdraw their

capital, it will be deemed presumptive evidence that the interest of the stockholders generally will be promoted by a dissolution of the company. In the *Matter of the Niagara Ins. Co.*, 1 Paige, 258 (1828). In *Stupart v. Arrowsmith*, 3 Sm. & G. 176 (1855), a bill filed by a shareholder on behalf of himself and others to set aside a dissolution, after three years acquiescence, no fraud or imposition being alleged, was dismissed with costs. *Cf. Kent v. Jackson*, 2 De G., M. & G. 49 (1852). *Denike v. New York, &c., Cement Co.*, 80 N. Y. 599, 606 (1880), where the court very explicitly says: "All the stockholders uniting might undoubtedly surrender the franchises of a corporation and work its dissolution. But can a portion of them do this in the absence of statutory authority? There is no statute in this State which authorizes a portion of the stockholders to maintain an action to dissolve a manufacturing corporation, and I know of no decision holding that they can." The action to dissolve must be brought by the attorney-general. *Wilmerdoerffer v. Lake Mahopac Improvement Co.*, 18 Hun, 387 (1879); *New York Laws of 1870*, chap. 151, § 2.

² *Kean v. Johnson*, 9 N. J. Eq. 401 (1853), where the court held that when the life of the corporation is limited in the charter, it must continue until the expiration of that time, unless, perhaps, in

authority for the same rule where the articles of association plainly militate against the idea of a dissolution by the majority.¹

§ 631. *Whether a minority may dissolve.*—Stockholders owning only a minority of the stock cannot, at common law, compel a dissolution before the expiration of the time limited in the charter for the existence of the corporation.² But where the company is insolvent, or is doing a ruinous business, with no reasonable prospect of a change, it has been held that a minority may force a dissolution, where the majority has the power to dissolve, but is unwilling to exercise that power.³ A court of equity has, in the absence of statutory power, no jurisdiction over corporations, for the purpose of decreeing their dissolution and the distribution of their assets among the individual corporators, at the suit of one or more of the stockholders.⁴ In Connecticut, by statute, a court of equity can dissolve a corporation only under certain specified circumstances. When, therefore, these circumstances do not exist, a bill filed by a stockholder for dissolution will be dismissed.⁵ In New York, the Supreme Court may, at

case of clear loss, and that if no time is fixed by the charter for the existence of the company, then the implied contract of the corporators with each other is that, so long as the officers of the company are prosperous, it shall go on, unless all consent to close up. *Van Schmidt v. Huntington*, 1 Cal. 55 (1850), which is the case of a New York joint-stock association organized for the purpose of mining in California. A provision in the articles prohibited a dissolution within one year after the arrival of the company in California. The court held that a portion of the company could not, under these circumstances, dissolve the corporation at their pleasure, but it appearing that the purpose of the organization could not be carried out, the court ordered a dissolution.

¹ *Black v. Delaware, &c., Canal Co.*, 22 N. J. Eq. 130, 403 *et seq.* (1871).

² *In re Joint Stock Coal Co.*, L. R. 8 Eq. 146 (1869); *In re London Suburban Bank*, L. R. 6 Chan. 641 (1871); *Fountain Ferry, &c. Co. v. Jewell*, 8 B. Mon. 140 (1848); *Gilman v. Greenpoint Sugar Co.*, 4 Lans. (N. Y.) 483 (1871). *Cf. Matter of Pyrolusite Manganese Co.*, 29 Hun,

429 (1883); *Denike v. New York, &c. Cement Co.*, 80 N. Y. 599 (1880).

³ *Re Factage Parisien Limited*, 34 L. J. Chan. 140 (1865); s. c. 13 W. R. 214, 330; *Re Great Northern Copper Mining Co.*, 17 W. R. 462 (1869); *Marr v. Union Bank*, 4 Coldw. (Tenn.) 484; *Masters v. Eclectic Life Ins. Co.*, 6 Daly, 455 (1876), where, however, the power was given by statute.

⁴ *Strong v. McCagg*, 55 Wis. 624 (1882); *Neall v. Hill*, 16 Cal. 145 (1860); *Bayless v. Orne*, 1 Freem. Chan. (Miss.) 161 (1843); *Belmont v. Erie Ry. Co.*, 52 Barb. 637 (1869); *Howe v. Deuel*, 43 Barb. 504 (1865); *Latimer v. Eddy*, 46 Id. 61 (1864); *Fountain Ferry, &c. Co. v. Jewell*, 8 B. Mon. 140 (1848); *Verplanck v. Mercantile Ins. Co.*, 1 Edw. Chan. 84 (1831). See New York Laws of 1870, ch. 151; New York Rev. Stat. vol. 2, pp. 462, 463. See § 634, *infra*. *Cf. Galwey v. United States, &c. Refining Co.*, 13 Abb. Prac. 211 (1861); s. c. 36 Barb. 256; *Ramsey v. Erie Ry. Co.*, 7 Abb. Prac. (N. S.) 156, 181 (1869); *Baker v. Backus*, 36 Ill. 79 (1863); *Follett v. Field*, 30 La. Ann. 161 (1878).

⁵ *Hardon v. Newton*, 14 Blatchf. 376 (1878).

the suit of the attorney-general, dissolve corporations, but the jurisdiction is statutory.¹ But the courts of that State have no jurisdiction over a foreign corporation so as to compel a distribution of the assets among the stockholders, even when the trustees are resident there.² In England, proof of the impossibility of carrying on the contemplated business would justify a winding up order upon petition of a minority of the shareholders, even in the absence of insolvency.³ In Massachusetts it is held that neither a court of law, nor a court of equity, can decree a dissolution at the suit of a single shareholder.⁴

§ 632. But corporate insolvency is generally held to be a good ground for dissolution.⁵ Insolvency as a ground of dissolution,

¹ 2 N. Y. Rev. Stat. 463, § 38; Laws of 1870 (New York), chap. 151, § 2; *Denike v. New York, &c. Cement Co.*, 80 N. Y. 599 (1880); *Wilmersdörffer v. Lake Mahopac Improvement Co.*, 18 Hun, 387 (1879). Cf. *Attorney General v. Bank of Chenango*, 1 Hopkins' Chan. (N. Y.) 596 (1826).

² *Redmond v. Enfield Manfg. Co.*, 13 Abb. Prac. (N. S.) 332 (1872). But they may appoint a receiver of such a corporation. *Murray v. Vanderbilt*, 39 Barb. 140 (1863).

³ *In re Suburban Hotel Co.*, L. R. 2 Chan. 737 (1867). In this case, however, Cairns, L. J. said: "I am, therefore, unable to find that any larger rule has been laid down, and I certainly do not think it desirable now to lay down a larger rule than that laid down by Lord Cottenham, and followed by the Master of the Rolls, in the case of *The Anglo-Greek Steam Company*, that if there be insolvency, or anything which is equivalent to a test of insolvency, if there be the circumstances that the company has not for a certain time commenced business, or has suspended business, that is a test given to the court by which to prove that the business cannot be carried on, and in those cases the company may be wound up. It is not necessary now to decide it; but if it were shown to the court that the whole substratum of the partnership, the whole of the business which the company was incorporated to carry on, has become impossible, I apprehend that the court might, either under the Act of Parliament, or on general principles, order the company to be wound up. But what I am prepared to hold is this: that this court, and the winding-up process of

the court, cannot be used, and ought not to be used, as the means of evoking a judicial decision as to the probable success or non-success of a company as a commercial speculation. This company may become successful, or may continue to be unprofitable, as I believe it has hitherto been; and it may, therefore, hereafter reappear in this court under different circumstances, but it is not for this court now to pronounce and, above all, not for this court to pronounce on opinion evidence, that this is likely to be an unprofitable speculation; and that, therefore, at the wish of a minority of shareholders, against the will of a large majority, the company should be wound up and put an end to." Cf. *In re Tumacacori Mining Co.*, L. R. 17 Eq. 534 (1874).

⁴ *Folger v. Columbian Ins. Co.*, 99 Mass. 267 (1868). But see the cases in the following note.

⁵ *State v. Bank of South Carolina*, 1 Spear (S. C.), 433, 451, 466 (1843); *Commercial Bank of Natchez v. State*, 14 Miss. 599, 617 (1846); *Planters' Bank, &c. v. State*, 15 Id. 163 (1846); *State v. Real Estate Bank*, 5 Ark. 595 (1844); *People v. Washington Bank*, 6 Cowen, 210, 216 (1826); *People v. Bank of Hudson*, 6 Id. 217 (1826); *State v. Seneca Co. Bank*, 5 Ohio St. 171 (1855). *Contra*, *State v. Bailey*, 16 Ind. 46, 51 (1861). Cf. *Ferris v. Strong*, 3 Edw. Chan. (N. Y.) 127 (1837). The fact that a corporation is insolvent will not authorize it to apply to a court of equity for a receiver to wind up its affairs. The receiver should be appointed only at the instance of the creditor. *Hugh v. McRae*, Chase's Dec. 466 (1869). Cf. *People v. Erie Ry. Co.*, 36 How. Prac. 129 (1868).

means inability to pay debts that are due. Accordingly, a court will not order a company to be wound up by reason of any liabilities not immediately payable, unless it is reasonably certain that the existing and probable assets will be insufficient to meet the existing liabilities. In no case will an account be taken of the possible liabilities or profits which may accrue in respect of future business.¹ When the circumstances are such as to warrant a forfeiture, it has been held that any stockholder may institute proceedings to that end,² but it is doubtful whether this can be considered good law. A virtual dissolution, but not a dissolution in law, occurs when the corporation is enjoined from the exercise of the corporate functions, or deprived of its property, by injunction and a decree appointing a receiver. And again, if the corporation ceases to do business, or complete the enterprise for which the incorporation was effected, or if it becomes impossible to carry on the corporate business, then a single shareholder may apply to a court of equity for a winding up of the corporation.³ But it has been held that, even though the corporation is inert and the officers do not act, and have all become non-residents, still it is not competent for a few stockholders to commence an action for a receiver and division of the corporate assets.⁴ And the mere misconduct of the corporate officers will not authorize a dissolution at the suit of a minority of stockholders.⁵ When a corporation is insolvent and the corporate officers are appointed by the stockholders to wind it up, in the

¹ *In re European Life Assurance Society*, L. R. 9 Eq. 122 (1869). See also *Re Factage Parisien*, 34 L. J. Chan. 140; s. c. 13 W. R. 214, 330; *In re Great Northern Copper Mining Co.*, 17 W. R. 462 (1869); *Re Suburban Hotel Co.*, L. R. 2 Chan. 737 (1867); *In re Tumacacori Mining Co.*, L. R. 17 Eq. 534. *Cf. Masters v. Eclectic Life Ins. Co.*, 6 Daly, 455 (1876); *Hardon v. Newton*, 14 Blatchf. 376; *Hugh v. McRae*, Chase's Dec. 466.

² *Ward v. Sea Insurance Co.*, 7 Paige, 294 (1838). But see *Curien v. Santini*, 16 La. Ann. 27 (1861); *Polar Star Lodge v. Polar Star Lodge*, Id. 53 (1861).

³ *In re Suburban Hotel Co.*, L. R. 2 Chan. 737, 750 (1867); *Cramer v. Bird*, L. R. 6 Eq. 143 (1868); *In re Joint Stock Coal Co.*, L. R. 8 Eq. 146 (1869); *In re Suburban Bank*, L. R. 7 Chan. 641 (1871); *Pratt v. Jewett*, 9 Gray, 34 (1857).

⁴ *Croft v. Lumpkin Chestatee Mining Co.*, 61 Ga. 465 (1878). But *cf. Ver-*

planck v. Mercantile Insurance Co., 1 Edw. Chan. (N. Y.) 84 (1831).

⁵ *Waterbury v. Merchants' Union Express Co.*, 50 Barb. 157 (1867); *People v. Albany, &c. R. R. Co.*, 55 Barb. 344 (1869); *Belmont v. Erie Ry. Co.*, 52 Id. 637 (1869). It is, however, no ground for dissolving a corporation, on a petition of a majority in numbers of the stockholders who, however, own but a minority of the stock, that one who owns a majority of the stock controls the elections, makes himself the manager and general agent of the concern, and conducts the business as he pleases, that, according to his reports, the business has not been prosperous, that he refuses to make any change in the manner of conducting it, or to buy the shares of the petitioners, and that under a different management the business could be made profitable. *Pratt v. Jewett*, 9 Gray, 34 (1857). The *Wabash Ry. Case*, U. S. C. C. Ill. Dec. 1886.

absence of an allegation of fraud, no court can step in and appoint a receiver to take possession of the property and conduct the business of closing up the affairs.¹ But if the majority of the stockholders neglect or refuse to act in the premises, the corporation being defunct and insolvent, a receiver may be appointed to wind it up.² Upon a voluntary dissolution of a corporation, any of its officers or stockholders may be appointed receivers if not otherwise disqualified.³ But the corporate officers or directors have no power, without authority from the stockholders, to take steps to dissolve the corporation.⁴ All the stockholders need not, however, be made parties to a dissolution suit which is regularly brought.⁵ When the corporate business is ended, the stockholders are entitled as a matter of right to a dissolution of the corporation.⁶

§ 633. *What will and what will not operate to dissolve.*—

There are certain acts or omissions of the shareholders which, while they may impair the free exercise of the corporate functions, and expose the corporation to an action on the part of the State for a dissolution or forfeiture of the franchises, do not in themselves constitute a dissolution. Thus, a failure to elect corporate officers at the time prescribed in the charter or by-laws, does not work a dissolution of the corporation.⁷ Nor will a resig-

¹ Follett v. Field, 30 La. Ann. 161 (1878).

² Lawrence v. Greenwich Fire Ins. Co., 1 Paige, 587 (1829).

³ In the Matter of the Eagle Iron Works, 8 Paige, 385 (1840). See § 2429, N. Y. Code of C. P.

⁴ Ward v. Sea Insurance Co., 7 Paige, 294 (1838); Abbot v. American Hard Rubber Co., 33 Barb. 578 (1861).

⁵ Von Schmidt v. Huntington, 1 Cal. 55 (1850).

⁶ Frothingham v. Barney, 6 Hun, 366 (1876); Taylor v. Earle, 8 Id. 1 (1876); McVicker v. Ross, 55 Barb. 247 (1869).

⁷ Rose v. Turnpike Co., 3 Watts (Penn.), 46 (1834); Lehigh Bridge Co. v. Lehigh Coal & Navigation Co., 4 Rawle (Penn.), 8, 23 (1832); Commonwealth v. Cullen, 13 Penn. St. 133 (1850); Hoboken Building, &c., Association v. Martin, 13 N. J. Eq. 427 (1861); Everts v. Killingworth Manfg. Co., 20 Conn. 447 (1850); Nashville Bank v. Petway, 3 Humph. (Tenn.) 522 (1842); Boston Glass Manfg. Co. v. Langdon, 24 Pick. 49 (1834); Russell v. McLellan, 14 Id. 63 (1833); Cahill v. Kalamazoo, &c., Ins. Co., 2 Doug. (Mich.)

124, 140 (1845); Harris v. Mississippi Valley, &c., R. R. Co., 51 Miss. 602 (1875), where the court say: "This allegation assumes that by reason of the non-election of the board of directors (within the time stated) the corporation has been dissolved. The legislature, in the particulars of the charter referred to, has very carefully guarded against that consequence. The rule is that a corporation is dissolved when it has lost the power of perpetuating itself; when (according to its nature), from the loss of its chief officer, or an integral part, and in its imperfect state, it has not the capacity to resuscitate or restore itself by a new election. So long as there remains the capacity of reviving restoration, it is not dead. Angell & Ames Corp., §§ 768, 769. No loss of members destroys a corporation so long as a sufficient number remain to continue the succession and fill up vacancies. Nor does the mere failure of the trustees or directors to meet dissolve the body. State v. Trustees Vincennes University, 5 Ind. 80, 81. That case, both in the questions of law and fact, is very similar

nation of all the officers have that effect.¹ The corporate rights and franchises are, in such a case, merely dormant until other officers are elected.² Again, the sale and assignment of all the corporate property will not necessarily dissolve the corporation, or operate as a surrender of the franchises.³ The fact that one person owns all the stock does not affect the corporate existence,⁴

to this. The point ruled was, if enough trustees remained to fill up vacancies and restore the corporation to vitality, although the board may not have kept up its regular meetings, the corporation was not dissolved." *s. r. People v. Runkle*, 9 Johns. 147 (1812); *Philips v. Wickham*, 1 Paige, 590 (1829); *Slee v. Bloom*, 5 Johns. Chan. 366 (1821); *s. c.*, 19 Johns. 456 (1822); *St. Louis, &c., Loan Association v. Augustin*, 2 Mo. Appeal, 123 (1876); *Knowlton v. Ackley*, 8 Cush. 93 (1851); *People v. Wren*, 5 Ill. 269 (1843); *President & Trustees, &c. v. Thompson*, 20 Id. 197 (1858). *Cf. Smith v. Smith*, 3 Desauss. (S. C.) 557 (1813); *Ward v. Sea Insurance Co.*, 7 Paige, 294 (1838); *People v. Twaddell*, 18 Hun, 427 (1879). In *Blake v. Hinkle*, 10 Yerg. (Tenn.) 218 (1836), the court said: "By the charter of the bank, granted in 1815, the existence of the corporation will continue till the year 1841. No dissolution is alleged in the bill, as the result of judicial or legislative action, but the corporation is stated to have been dissolved by the non-election of officers and other acts inconsistent with the charter. The failure to elect directors or other officers could not produce a dissolution of the corporation, nor could it prevent the institution of an action at law. For it is provided, with regard to this bank, by the act of 1821, c. 197, § 5, that, in such event, demand shall be made and process served upon the late president, cashier, or any director." It seems that it makes no difference whether the old officers are authorized to hold over or not, and the rule is the same in public and private corporations. *Philips v. Wickham*, 1 Paige, 590 (1829); *People v. Wren*, 5 Ill. 269 (1843).

¹ *Muscatine Turn Verein v. Funck*, 18 Iowa, 469 (1865); *Everts v. Killingworth Manfg. Co.*, 20 Conn. 447 (1850).

² *Philips v. Wickham*, 1 Paige, 590 (1829). *Cf. Lea v. American Atlantic, &c., Canal Co.*, 3 Abb. Prac. (N. S.) 1 (1867).

³ *Barclay v. Talman*, 4 Edw. Chan. 123 (1842); *De Camp v. Aylward*, 52 Ind. 468 (1876); *Richwald v. Commercial Hotel Co.*, 106 Ill. 439 (1883); *Rollins v.*

Clay, 33 Me. 132 (1851); *Kansas City Hotel Co. v. Sauer*, 65 Mo. 279 (1877); *Troy, &c., R. R. Co. v. Kerr*, 17 Barb. 581 (1854). In *State v. Merchant*, 37 Ohio St. 251 (1881), it was held that the right of stockholders of a railway company to meet and elect directors of the corporation is not affected by the sale of the property of the company by a receiver under an order of the court. The court said: "The appointment of the receiver and the sale of the property of the railway company have no bearing on the question before us. These facts did not work a dissolution of the corporation, and while the corporation continued it was competent for the stockholders to elect directors." *Robertson, C. J.*, in *Smith v. Gower*, 2 Duval, 17 (1865), said: "The sale of the road neither passed to the purchaser the liabilities of the appellants, nor destroyed the corporation. The corporate existence of the company still continued for more than one purpose, and certainly for the purpose of collecting and paying its debts." *Acc. State v. Rives*, 5 Ired. Law (N. C.), 297 (1844); *Bruffett v. Great Western R. R. Co.*, 25 Ill. 353 (1861).

⁴ *Newton Manfg. Co. v. White*, 42 Ga. 148 (1871), where the court say: "The fact that in an association under the act of 1847, one of the stockholders finally buys up and owns all the stock and property of the balance, and the whole lodges in him, does not deprive such person from the use and rights of the charter to carry on the business under the name adopted; and the fact of being the sole owner, if he goes on and uses such name, does not abate suits at law or equity filed against such corporation, although individual property. No corporation, once legally existing, dies, in contemplation of law, without some act forfeiting its franchises; but it will be recognized by the law as long as it carries on its legitimate business in its corporate name, and through agents and persons who use that name in its trade or business. It would be an anomalous doctrine that one should purchase all the stock of such a joint-

nor is the corporation dissolved by a cessation of all corporate acts.¹ But a foreclosure sale of all the property and franchises of a corporation will close out and foreclose the whole interest of the stockholders therein.² There may, however, be a valid agreement between a railway corporation, the mortgagees in trust of its road, and the bondholders, that after a sale under the mortgage the company should be so reorganized that the stockholders and unsecured creditors of the old company should become stockholders in the new company. Such an agreement would modify to that extent the effect of the mortgage sale.³ In general, a corporation having capital stock does not suffer dissolution by reason of the death of all its members, since the stock passes at once to their legatees or distributees.⁴ Nor is insolvency in itself dissolution,⁵ even though a receiver has been appointed.⁶ When two or more corporations are consolidated or amalgamated, such consolidation or amalgamation may operate to dissolve the original

stock company privately, and, without giving notice of such ownership, should carry on the business, use the corporate name, brands, stamps, and trade-marks, and keep books in its name, buy and sell in its name, and be permitted to plead its dissolution when sued by the very name in which it contracted, in violation of the terms of its existence that it could sue and be sued by that name. Every corporation speaks by men, and its artificial existence blends with that of its agents and officers. The corporate name is nothing without the living men who use that name; but when used by those who are its proper agents, it is liable by that name to suit under the provisions of its charter." See also *Sharp v. Dawes*, 46 L. J. (Q. B.) 104 (1876); *Button v. Hoffman*, 61 Wis. 20 (1884); *Swift v. Smith* (Md., 1886), 6 East. Rep. 574; *England v. Dearborn*, 141 Mass. 590 (1886); *Hopkins v. Roseclare Lead Co.*, 72 Ill. 373 (1874). The rule is the same where two persons buy all the stock. *Russell v. McLellan*, 14 Pick. 63 (1833). The corporation still subsists, and the two purchasers do not become partners, or joint-tenants, or tenants in common of the corporate property. Cf. *Commonwealth v. Cullen*, 13 Penn. St. 133 (1850).

¹ *Attorney-General v. Bank of Niagara*, *Hopkins' Chan.* (N. Y.) 403 (1825); *Baptist Meeting House v. Webb*, 66 Me. 398 (1877); *Rollins v. Clay*, 33 Me. 132 (1851); *Harris v. Nesbit*, 24 Ala. 398 (1854);

Kansas City Hotel Co. v. Sauer, 65 Mo. 279, 288 (1877); *Nimmons v. Tappan*, 2 Sweeney (N. Y.), 652 (1870); *Mickles v. Rochester City Bank*, 11 Paige, 118 (1844); *State v. Barron*, 58 N. H. 370 (1878); *Troy, &c., R. R. Co. v. Kerr*, 17 Barb. 581 (1854). Cf. *Re Jackson Marine Ins. Co.*, 4 Sandf. Chan. (N. Y.) 559 (1847); *Conro v. Gray*, 4 How. Prac. 166 (1849). See also 2 Rev. Stat. of N. Y. 463, 464, §§ 38, 56.

² *Vatable v. New York, &c., R. R. Co.*, 96 N. Y. 49 (1884); *Thornton v. Wabash Ry. Co.*, 81 Id. 462, 467 (1880). Cf. *Mickles v. Rochester City Bank*, 11 Paige, 118, 127 (1844); *Sullivan v. Portland & Kennebec R. R. Co.*, 94 U. S. 806 (1876).

³ *Smith v. Chicago, &c., R. R. Co.*, 18 Wis. 17 (1864).

⁴ *Boston Glass Manfg. Co. v. Langdon*, 24 Pick. 49, 52 (1834); *Russell v. McLellan*, 14 Pick. 63, 69 (1833). Cf. *Chesapeake & Ohio Canal Co. v. Baltimore, &c., R. R. Co.*, 4 Gill & J. 1, 121.

⁵ *Moseby v. Burrow*, 52 Texas, 396 (1880); *Valley Bank & Savings Institution v. Sewing Society*, 28 Kan. 423 (1882).

⁶ *State v. Merchant*, 37 Ohio St. 251 (1881); *Taylor on Corporations*, § 433. A national bank in voluntary liquidation, under § 5220 of the Revised Statutes, is not thereby dissolved as a corporation, but may sue and be sued for the purpose of winding up its business. *National Bank v. Insurance Co.*, 104 U. S. 54 (1881).

corporations, or it may not. Generally, as it seems, the consolidation operates to dissolve the old corporation, but this is not universally the case.¹

§ 634. *Statutes regulating dissolution.*—There are in nearly all of the States, statutes which regulate the dissolution of incorporated companies, and prescribe in detail the formalities to be observed in a winding up.² They usually contain a provision that the corporate existence shall be continued for a fixed time, pending the proceedings for dissolution, so that suits may be brought by and against the corporation for the purpose of closing the business and disposing of the assets.³ Under

¹ In Ohio, the consolidation of two or more railway companies, pursuant to the statute of April 10, 1856 (4 Curwen, 2791), works their dissolution. *Shields v. Ohio*, 95 U. S. 319 (1877). This is also the case in Georgia. *Railroad Co. v. Georgia*, 98 U. S. 359 (1878); *Atlanta, &c., R. R. Co. v. State*, 63 Ga. 483 (1879). Where an Indiana and Ohio railway corporation were consolidated, it was held in Indiana that the Indiana corporation was dissolved, but that, for the purpose of enforcing the payment of a debt, the Ohio corporation would be assumed to be still in existence. *Eaton & Hamilton R. R. Co. v. Hunt*, 20 Ind. 457 (1863). Generally a consolidation works the dissolution of the old corporations. *Clearwater v. Meredith*, 1 Wall. 25, 40 (1863); *McMahon v. Morrison*, 16 Ind. 172 (1861); *State v. Bailey*, 16 Id. 46 (1861); *Powell v. North Missouri R. R. Co.*, 42 Mo. 63 (1867); *Racine, &c., R. R. Co. v. Farmers Loan & Trust Co.*, 49 Ill. 331, 349 (1868). But each case depends upon its own peculiar circumstances, and the rule is by no means a universal one. In *Wabash, &c., R. R. Co. v. Ham*, 114 U. S. 587, 595 (1884), the court said: "But upon the consolidation, under express authority of statute, of two or more solvent corporations, the business of the old corporations is not wound up, nor their property sequestered or distributed, but the very object of the consolidation and of the statutes which permit it is to continue the business of the old corporations. Whether the old corporations are dissolved into the new corporation, or are continued in existence under a new name and with new powers; and whether, in either case, the consolidated company takes the property of each of the old corporations, charged with a lien for the pay-

ment of the debts of that corporation, depend upon the terms of the agreement of consolidation, and of the statutes under whose authority that consolidation is effected." See also *State v. Merchant*, 37 Ohio St. 251 (1881); *Prouty v. Lake Shore, &c., R. R. Co.*, 52 N. Y. 363 (1873).

² Massachusetts—Gen. Stat., chap. 68, §§ 35–39. Iowa—Code, § 1074. Illinois—Rev. Stat., p. 577, § 25. Ohio—Act of May 1, 1852 (3 Curwen, 1876). Alabama—Code, § 1775 *et seq.* New York—2 Rev. Stat., 461, 484, §§ 39–41; Laws of 1849, chap. 226; 1 Rev. Stat., 600 (7th ed., 1830); Code of Civil Procedure, §§ 1785, 1786, 2419 *et seq.* Pennsylvania—Brightley's Purdon's Digest (1862), 197; *In re Franklin Telegraph Co.*, 119 Mass. 447 (1876); *Fisher v. World, &c., Life Ins. Co.*, 15 Abb. Prac. (N. S.) 363 (1873); *People v. Central City Bank*, 53 Barb. 412 (1867); *Mooney v. British, &c., Life Ins. Co.*, 9 Abb. Prac. (N. S.) 103 (1869); *Matter of Pyrolusite Manganeses Co.*, 29 Hun, 429 (1883); *In the Matter of DuBois*, 15 How. Prac. 7 (1856); s. c. *sub nom.* *Case of the Westchester Iron Co.*, 6 Abb. Prac. 386, note. In California there is no statutory provision for the dissolution of corporations for literary purposes, having no stockholders. Accordingly, upon the disincorporation of such a corporation, if it owe no debts, all its personal estate, and all its real property, acquired by purchase for value, vests by operation of law in the State. *People v. President & Trustees of the College of California*, 38 Cal. 166 (1869).

³ *Stetson v. City Bank of New Orleans*, 12 Ohio St. 577 (1861); *McGoon v. Scales*, 9 Wall. 23 (1869); *Mariners Bank v. Sewall*, 50 Me. 220 (1861); *Muscantine Turn Verein v. Funck*, 18 Iowa, 469 (1865);

statutes in some of the States an information in the nature of *quo warranto* may be filed at the relation of a shareholder against an illegally existing corporation, to compel a dissolution.¹ And in some jurisdictions there are provisions for the appointment of receivers to wind up the business.² By the National Banking Act it is provided that a national bank "may go into liquidation and be closed by the vote of its shareholders, owning two-thirds of the stock." This liquidation is effected through a receiver, appointed by and acting for the comptroller of the currency.³ The statute provides in detail the mode of procedure, and the duties of the receiver in such cases.⁴ The statutory liability of the shareholders in incorporated companies, for the debts of the concern, upon a dissolution, is considered elsewhere.⁵

§ 635. *The English statute.*—In England, there is a statute providing for the winding up of companies known as "the winding up act,"⁶ under which the business, not only of corpora-

Thornton v. Marginal Freight Ry. Co., 128 Mass. 32 (1877); Folger v. Chase, 18 Pick. 63 (1836); Crease v. Babcock, 10 Metc. 525, 567 (1846); *Re Independent Ins. Co.*, 1 Holmes, 103; Franklin Bank v. Cooper, 36 Me. 179; Nevitt v. Bank of Port Gibson, 14 Miss. 513 (1846). The life of the corporation is frequently extended by these statutes for three years. Herron v. Vance, 17 Ind. 595 (1861); Foster v. Essex Bank, 16 Mass. 245 (1819); Blake v. Portsmouth, &c., R. R. Co., 39 N. H. 435 (1859); Van Glahn v. De Rosset, 81 N. C. 467 (1879); Michigan State Bk. v. Gardner, 15 Gray, 362 (1860). Sometimes five years. Tuscaloosa, &c., Association v. Green, 48 Ala. 346 (1872). In Herron v. Vance, *supra*, the court says: "The question, therefore is, whether these statutes confer authority to sue in this case in the name of the receiver, and if so, whether enough is shown in the complaint? In this connection it may throw some light, in giving the proper construction, to notice the twelfth section of an act establishing general provisions respecting corporations. 1 R. S., p. 239, that provides where the charter of a corporation shall expire, that within three years the proper court shall, on application, &c., appoint a receiver, or trustee, to take charge of the estate, eff cts, &c., 'with power to prosecute and defend, in the name of the corporation or otherwise, all suits, &c.' And the sixth section of

the same act continues, as bodies corporate for three years, all corporations whose 'charters shall expire by limitation, forfeiture, or otherwise,' to enable them to prosecute and defend suits, settle, &c. Taking these two sections together, it is apparent that all corporations organized under the provisions of that act, are, for certain purposes, considered as in being for three years after they shall have ceased to legally exist, for the purpose of their organization; that is, that the affairs of said corporation may be properly closed up, if necessary, by suits to be conducted in the name of the defunct body, which the law makers appear, perhaps correctly, to have thought could not be done without an act upon the subject." *Cf.* Lincoln, &c., Bank v. Richardson, 1 Me. 79 (1820).

¹ Albert v. State, 65 Ind. 413 (1879).

² So in Connecticut—Lothrop v. Stedman, 13 Blatchf. 134, 143 (1875). New York—Owen v. Smith, 31 Barb. 641 (1861). North Carolina—Van Glahn v. De Rosset, 81 N. C. 467 (1879).

³ Rev. Stat. of U. S., 1873-74, tit. 62, chap. 4, § 5220.

⁴ Kennedy v. Gibson, 8 Wall. 498 (1869); Bank of Bethel v. Palquique Bank, 14 Wall. 383 (1870); Bank v. Kennedy, 17 Wall. 19 (1872); *In re Platt, Receiver*, 1 Benedict, 534 (1867).

⁵ See Chap. XII, *supra*.

⁶ Stat. 25 & 26 Vict. chap. 89, § 129.

tions, but also of the English joint-stock companies, is closed up, upon prescribed conditions, by a voluntary dissolution.¹

§ 636. *A lease or transfer of corporate property and franchises as a means of dissolution.*—A corporation is sometimes formally dissolved for the purpose of transferring its assets to another corporation. In such a case, payment for the property and franchises of the old corporation is occasionally made, not in cash, but in the stock of the new corporation. When this is done, it is a settled rule that the shareholders of the old corporation cannot be compelled to accept such a payment.² Such of them as do not voluntarily join the new corporation are entitled

¹ The material parts of act are as follows: "A company under this act may be wound up voluntarily.

"(1.) Whenever the period, if any, fixed for the duration of the company by the articles of association expires, or whenever the event, if any occurs, upon the occurrence of which it is provided by the articles of association, that the company is dissolved, and the company in general meeting has passed a resolution requiring the company to be wound up voluntarily.

"(2.) Whenever the company has passed an extraordinary resolution to the effect that it has been proved to their satisfaction that the company cannot, by reason of its liabilities, continue its business, and that it is advisable to wind up the same." Stat. 25 & 26 Vict., chap. 89, § 129. See the following cases for a construction of the provisions of the above act. *In re Exmouth Docks Co.*, L. R., 17 Eq. 181 (1873); *In re Sanderson's Patents Association*, L. R., 12 Eq. 188 (1871); *In re Bradford Navigation Co.*, L. R., 10 Eq. 331 (1870); *Princess of Reuss v. Bos*, L. R., 5 H. of L. 176 (1871); *In re Commercial Bank of India*, L. R., 6 Eq. 517 (1868); *In re London India Rubber Co.*, L. R., 1 Chan. 329 (1866); *In re Pen-y-Van Colliery Co.*, L. R., 6 Chan. Div. 477 (1877); *In re United Service Co.*, L. R., 7 Eq. 76 (1868).

² *In re Empire Assurance Corporation*, L. R., 4 Eq. 341 (1867), where the court says: "I think it is impossible to give to the word 'amalgamate' the force which is contended for. It is difficult to say what the word 'amalgamate' means. I confess at this moment I have not the least conception of what the full legal

effect of the word is. We do not find it in any law dictionary, or expounded by any competent authority. But I am quite sure of this, that the word 'amalgamate' cannot mean that the execution of a deed shall make a man a partner in a firm in which he was not a partner before, under conditions of which he is in no way cognizant, and which are not the same as those contained in the former deed. It is true that in this instance partners, engaged in a concern for insurance of a particular character, have authorized their directors to amalgamate with another company. It is possible that this authority may go thus far. . . In carrying out this, the directors may possibly be authorized by the clause to say, 'you who do not like this arrangement must simply lose; we have amalgamated one company with the other' (which seems to be a process of annihilation or extinction, rather than anything else), 'and we have placed all your assets in the hands of another concern.' But that does not imply that the dissentient shareholders, besides losing all their assets, are personally bound to take their part and lot in the new concern. It is one thing to say (not 'probably,' but), 'possibly you may find all the assets gone, and your shares of no value;' but it is a prodigious step further to say that a dissentient shareholder, having been concerned in an insurance company, shall be obliged to become subject to all the liabilities of another company." s. r. Clinch v. Financial Corporation, L. R., 4 Chan. 117 (1868); *State v. Bailey*, 16 Ind. 46 (1861); *Lauman v. Lebanon Valley R. R. Co.*, 30 Penn. St. 42 (1858).

to the value of their shares in the old corporation in cash, and may have an injunction until they are secured.¹ To compel the stockholders of the old corporation to accept the stock of the new corporation in payment for their interest in the old, would be in effect to compel them to join the new corporation, or what is the same thing, to compel them to consent to the consolidation.² The old corporation may, however, lawfully accept payment for its assets in shares of stock in the new corporation, and may then distribute that stock ratably among such of the old stockholders as are willing to accept it, selling the rest of the shares and paying to the remainder of the old stockholders cash, to the extent of their interest in the assets of the old corporation.³

When the regular business of the corporation has been brought to a close the shareholders have a right to an immediate distribution of the corporate assets.⁴ They cannot, therefore, be compelled to accept other property or rights in lieu of cash. Accordingly, a lease of the company's property and franchises with an annual rent reserved to be distributed among the stockholders as a dividend, is not legal as against dissenting stockholders, unless provision is made for paying them the value of their stock in cash.⁵ Such a method of winding up the corporation is legal

¹ *State v. Bailey*, 16 Ind. 46 (1861); *Gratz v. Penn. R. R. Co.*, 41 Penn. St. 447 (1862); *Kelly v. Mariposa Land & Mining Co.*, 4 Hun, 632 (1875). *Cf.* *New Jersey Zinc Co. v. New Jersey Franklinite Co.*, 13 N. J. Eq. 322 (1861); s. c. 15 Id. 418 (1862).

² *Ex parte Bagshaw*, L. R., 4 Eq. 341 (1867); *Clinch v. Financial Corp.*, L. R., 4 Chan. 117 (1868); *Bird v. Bird's Patent, &c., Sewage Co.*, L. R., 9 Chan. 358 (1874); *McCurdy v. Meyers*, 44 Penn. St. 535 (1863); *Frothingham v. Barney*, 6 Hun, 366 (1876).

³ *Treadwell v. Salisbury Mfg. Co.*, 7 Gray, 392 (1856). *Cf.* *Wilson v. Proprietors of Central Bridge*, 9 R. I. 590 (1870). See also *Buford v. Keokuk Northern Line Packet Co.*, 3 Mo. App. 159 (1876); *Black v. Delaware, &c., Canal Co.*, 22 N. J. Eq. 130, 415 (1871); s. c. 24 Id. 455 (1873); *Lauman v. Lebanon Valley R. R. Co.*, 30 Penn. St. 42 (1858); *Middlesex R. R. Co. v. Boston, &c., R. R. Co.*, 115 Mass. 347, 351 (1874); *Conro v. Port Henry Iron Co.*, 12 Barb. 27 (1851); *Gratz v. Penn. R. R. Co.*, 41 Penn. St.

447; *Winch v. Birkenhead, &c., R. R. Co.*, 5 DeG. & Sm. 562 (1852); *Midland Ry. Co. v. Great Western Ry. Co.*, L. R., 8 Chan. 841 (1873); *Featherstonhaugh v. Lee Moor Porcelain Clay Co.*, L. R., 1 Eq. 318 (1865).

⁴ *Frothingham v. Barney*, 6 Hun, 366 (1876); *Taylor v. Earle*, 8 Id. 1 (1876); *McVicker v. Ross*, 55 Barb. 247 (1869). In these cases it is intimated that, upon a dissolution, the stockholders are entitled to a public sale of the assets as distinguished from a lease or consolidation.

⁵ *Black v. Delaware, &c., Canal Co.*, 24 N. J. Eq. 455 (1873); *Middlesex R. R. Co. v. Boston, &c., R. R. Co.*, 115 Mass. 351 (1874); *State v. Bailey*, 16 Ind. 46 (1861); *Conro v. Port Henry Iron Co.*, 12 Barb. 27 (1851); *Gratz v. Penn. R. R. Co.*, 41 Penn. St. 447; *Winch v. Birkenhead, &c., R. R. Co.*, 5 DeG. & Sm. 562 (1852); *Midland Ry. Co. v. Great Western Ry. Co.*, L. R., 8 Chan. 841 (1873). *Cf.* *Featherstonhaugh v. Lee Moor Porcelain Clay Co.*, L. R., 1 Eq. 318 (1865).

only when every dissenting stockholder is given the full value of his interest in the corporate property in cash.¹ A court of equity will not interfere with a voluntary winding up unless there be fraud or an inequitable overbearing of the rights of a dissenting minority.² There are a few cases to the effect that a dissenting shareholder may prevent entirely such a dissolution and consolidation,³ but these cases seem to hold that such a dissolution is a fraud upon the stockholders and the law, in that a consolidation is thereby effected indirectly when it could not be effected directly.

§ 637. *Dissolution by legislative repeal or forfeiture, or by judicial forfeiture, or by lapse of time.*—The stockholders of a corporation have little or nothing to do with the dissolution of a corporation which is effected in any one of these methods. The assets after the dissolution belong to the stockholders and the corporate creditors. Yet the dissolution itself depends upon the will of the stockholders only when it is a voluntary dissolution. Nevertheless if, in effecting the dissolution in one of the other methods, a fraud is perpetrated on the stockholders, they are not without remedy. Thus a court of equity will, upon the application of a shareholder, open or vacate a judgment dissolving a corporation, even when the shareholder was not a party to the action instituted by the attorney-general, when there is reasonable ground to believe that there was fraud or collusion in

¹ *Black v. Delaware, &c., Canal Co.*, 24 N. J. Eq. 455 (1873); s. c. 22 Id. 130, 415 (1871); *Lauman v. Lebanon Valley R. R. Co.*, 30 Penn. St. 42 (1858); *In re United Ports & General Ins. Co.*, L. R., 8 Chan. 1002 (1873); *Perrett's Case*, L. R., 15 Eq. 250 (1873); *Ex parte Fox*, L. R., 6 Chan. 176, 184 (1871); *Bagshaw's Case*, L. R., 4 Eq. 341 (1867); *Clinch v. Financial Corporation*, L. R., 5 Eq. 450, 472; s. c. L. R. 4 Chan. 117. *Cf. In re Anglo-Greek Steam Co.*, L. R., 2 Eq. 1 (1866); *Clearwater v. Meredith*, 1 Wall. 25 (1863); *Nugent v. Putnam Co.*, 3 Biss. 105 (1871); *Nugent v. Supervisors*, 19 Wall. 241 (1873); *McMahan v. Morrison*, 16 Ind. 172 (1861); *Mowry v. Indiana, &c., R. R. Co.*, 4 Biss. 78.

² *In re Beaujolais Wine Co.*, L. R., 3 Chan. 15 (1876); *In re London & Mercantile Discount Co.*, L. R., 1 Eq. 277

(1865); *People v. Hektograph Co.*, 10 Abb. N. C. (N. Y.) 358 (1882); *Booth v. Bunce*, 33 N. Y. 139 (1865). *Cf. White Mountains R. R. Co. v. White Mountains, &c., R. R. Co.*, 50 N. H. 50 (1870); *Hodges v. New England Screw Co.*, 1 R. I. 312 (1850); s. c. 3 R. I. 1 (1853); *Rorke v. Thomas*, 56 N. Y. 559 (1874); *Barclay v. Quicksilver Mining Co.*, 9 Abb. Prac. (N. S.) 283 (1870); s. c. 6 Lans. 25 (1872). See also *Bronson v. La Crosse Ry. Co.*, 2 Wall. 283; *Mussina v. Goldthwaite*, 34 Texas, 125; *Shawhan v. Zinn*, 79 Ky. 300; *Young v. Moses*, 53 Ga. 628; *Talbot v. Scripps*, 31 Mich. 268; *Putnam v. Sweet*, 1 Chandler (Wis.), 286, 334.

³ *Kean v. Johnston*, 9 N. J. Eq. 407; *Zabriskie v. Hackensack, &c., R. R. Co.*, 18 Id. 178. See also *Lauman v. Lebanon, &c., R. R. Co.*, *supra*.

obtaining the judgment, operating to the injury of the shareholder.¹

§ 638. *The assets upon dissolution.*—Upon the dissolution of a corporation the corporate assets of every kind, after the payment of corporate debts belong to the shareholders, and are to be distributed among them proportionately according to the number of their shares.² At common law it was the rule that upon the dissolution of a body corporate its real estate reverted to the grantor, its personal property to the State or sovereign, and the debts due to it and from it were forgiven and extinguished.³

This rule arose at a time when private corporations for business purposes were comparatively unknown, and it had its origin in the disposition to limit the accumulation of property in the hands of the church. The injustice of its application in modern

¹ *People v. Hektograph Co.*, 10 Abb. N. C. (N. Y.) 358 (1882). See also the cases in note 2, p. 662.

² *Krebs v. Carlisle Bank*, 2 Wall. (C. C.) 33 (1850); *Heath v. Barmore*, 50 N. Y. 302 (1872); *Burrall v. Bushwick R. R. Co.*, 75 N. Y. 211 (1878); *James v. Woodruff*, 10 Paige, 541 (1844); *Frothingham v. Barney*, 6 Hun, 366 (1876); *Wood v. Dummer*, 3 Mason, 308, 322 (1824); *Dudley v. Price's Admr.*, 10 B. Mon. 84 (1849). See *Fish v. Nebraska City Barb Wire, &c., Co.*, 25 Fed. Rep. 795 (1885). *Cf. In re Hodges Distillery Co., L. R.*, 6 Ch. 51 (1870); *Thornton v. Marginal Freight Ry. Co.*, 123 Mass. 32 (1877); *Nathan v. Whitlock*, 9 Paige, 152 (1841); *Lea v. American Atlantic, &c., Canal Co.*, 3 Abb. Prac. (N. S.) 1 (1867); *Curren v. State of Arkansas*, 15 How. 304, 307 (1853); *Hastings v. Drew*, 76 N. Y. 9 (1879); affirming s. c. 50 How. Prac. 254 (1874); *Wilde v. Jenkins*, 4 Paige, 481 (1834).

³ *Hightower v. Thornton*, 8 Ga. 486 (1850); *Life Association of America v. Fassett*, 102 Ill. 315 (1883); *Commercial Bank v. Lockwood*, 2 Harr. (Del.) 8 (1835); *State v. Rives*, 5 Ired. (N. C.) 297 (1844); *White v. Campbell*, 5 Humph. (Tenn.) 38 (1844); *Fox v. Horah*, 1 Ired. Eq. (N. C.) 358 (1841); *Malloy v. Mallett*, 6 Jones Eq. (N. C.) 845 (1863); *President, &c., of Port Gibson v. Moore*, 21 Miss. 157 (1849); *Bingham v. Weiderwax*, 1 N. Y. 509 (1848); *Owen v. Smith*, 31 Barb. 641 (1860); *Miami, &c., Co. v.*

Gano, 13 Ohio St. 269; *State Bank v. The State*, 1 Blackf. (Ind.) 268 (1823); *Angell & Ames on Corp.*, § 779; *Coke on Litt.* 13 b. See also Proceedings between the King and the City of London, 8 Howell's State Trials, 1087 (1682); *Attorney-General v. Lord Gower*, 9 Mod. 224 (1740); *The King v. Pasmore*, 3 Term Rep. 199 (1789). The common law rule is harsh and inequitable, and has never been fully adopted or acted on in New York, and the rule was changed by statute [Act of April 9, 1811, 1 R. S. 248, 600, §§ 9, 10], for the relief of the creditors of the corporation. *Owen v. Smith*, 31 Barb. 641 (1860); *Bank of Mississippi v. Duncan*, 56 Miss. 166, 173 (1878), where the court said: "It was firmly settled by the decision of the High Court of Errors and Appeals of this State, that banks in this State were subject to the operation of the common law incidents to the dissolution of a corporation, *i.e.*, the extinction of all its rights and liabilities, except in so far as changed by statute. *Commercial Bank v. Chambers et al.* 8 Smed. & M. 9; *Coulter et al. v. Robertson*, 24 Miss. 278. And it was expressly declared that the right of stockholders were not preserved by the Act of July 26, 1843, but were left to their fate as at common law, which was to perish. *Coulter et al. v. Robinson*, 24 Miss. 278." *Cf.* with this case, *Bacon v. Robertson*, 18 How. (U. S.) 480 (1855); *Lum v. Robertson*, 6 Wall. 277 (1867); *Curran v. State of Arkansas*, 15 How. 304 (1853).

times to corporations having a capital stock is so palpable, that the courts refuse to recognize it, and in many of the States the rule is expressly abrogated by statute.¹ A court of equity will wholly disregard the rule of the common law, and treat the property and effects of the corporation upon dissolution as a trust fund for the payment of creditors and stockholders.² In some jurisdictions the common law rule still prevails as to land held by railway corporations, and in some other cases.³ And a few courts, upon general principles, still incline to uphold, though with evident reluctance, the common law rule in all its strictness.⁴ In

¹ *Robinson v. Lane*, 19 Ga. 337 (1856); *Lothrop v. Stedman*, 13 Blatchf. 134 (1875); *Blake v. Portsmouth, &c. R. R. Co.*, 39 N. H. 435 (1859); *Matter of Woven Tape Skirt Co.*, 8 Hun, 508 (1876); *Mumma v. Potomac Co.*, 8 Peters, 281 (1834); *Bacon v. Robertson*, 18 How. 480 (1855); *Lum v. Robertson*, 6 Wall. 277 (1867); *Read v. Frankfort Bank*, 23 Me. 318 (1843); *Newfoundland Ry. Construction Co. v. Schack*, 40 N. J. Eq. 222 (1885); *Fox v. Horah*, 1 Ired. Eq. (N. C.) 358 (1841); *Bingham v. Weiderwax*, 1 N. Y. 509 (1848); *Curry v. Woodward*, 53 Ala. 371 (1875); *New York Laws of 1876*, chap. 442. See *Hamilton v. Accessory Transit Co.*, 26 Barb. 416 (1857); *Commonwealth v. City of Boston*, 9 Gray, 451 (1857). The fee simple of lands in New York, appropriated for the use of the State canals, is in the State, and there is no reversion in the former owner, upon an abandonment of the public use. *Rexford v. Knight*, 11 N. Y. 308 (1854), affirming s. c. 15 Barb. 627. Cf. *Commonwealth v. Fisher*, 1 Penr. & W. (Penn.), 462 (1830); *Plitt v. Cox*, 43 Penn. St. 486 (1862). *Contra*, *State v. Rives*, 5 Ired. (N. C.) 297 (1844). So also of lands taken under the right of eminent domain for public parks. *Brooklyn Park Commissioners v. Armstrong*, 45 N. Y. 234 (1871); reversing s. c. 3 Lans. 429; *De Varaigne v. Fox*, 2 Blatchf. 95 (1848); *Heyward v. City of New York*, 7 N. Y. 314 (1852); *Dingley v. City of Boston*, 100 Mass. 544 (1868); *Haldeman v. Penn. R. R. Co.*, 50 Penn. St. 425 (1865), or lands conveyed to a religious corporation. *Towar v. Hale*, 46 Barb. 361 (1866). And the common law rule that real estate held by a corporation at the time of its dissolution reverts to the grantor, does not any longer prevail. Accordingly, where land

is conveyed absolutely to a corporation having stockholders, no reversion or possibility of reverter remains in the grantor. *Heath v. Barmore*, 50 N. Y. 302 (1872).

² *Powell v. North Mo. R. R. Co.*, 42 Mo. 63 (1867); *Wood v. Dummer*, 3 Mason, 308 (1824); *Lum v. Robertson*, 6 Wall. 277 (1867). See *Murray v. Vanderbilt*, 39 Barb. 140 (1863). In *Ingraham v. Terry*, 11 Humph. (Tenn.) 572 (1851), it was held that the dissolution of a corporation by the expiration of its charter works an abatement of a suit pending for the recovery of debts due to the corporation, in the absence of legislative provision for such contingency. *Acc.* *Greeley v. Smith*, 3 Story C. C. 657 (1845). *Contra* *McCoy v. Farmer*, 65 Mo. 244 (1877); *Life Association of America v. Fassett*, 102 Ill. 315 (1882). Cf. *Saltmarsh v. Planters, &c. Bank of Mobile*, 17 Ala., 761 (1850); *Carey v. Giles*, 10 Ga. 9 (1851); *Merrill v. Suffolk Bank*, 31 Me. 57 (1849). It was formerly held in Delaware, that it was not within the power of the legislature, by renewing a charter, to revive the liabilities of a corporation when they had been cancelled by dissolution. *Commercial Bank v. Lockwood*, 2 Harr. (Del.) 8, 183 (1835). *Contra*, *Colchester v. Seaber*, 3 Burr. 1866 (1766); *Erie, &c. R. R. Co. v. Casey*, 26 Penn. St. 287 (1856).

³ *State v. Rives*, 5 Ired. (N. C.) 297 (1844); *Acklin v. Paschal*, 48 Texas, 147 (1877); *St. Philip's Church v. Zion, &c. Church*, 23 S. C. 297 (1885). Cf. *Hopkins v. Whitesides*, 1 Head, 31. But see *Erie, &c. R. R. Co. v. Casey*, 26 Penn. St. 287 (1856).

⁴ *St. Philip's Church v. Zion, &c. Church*, 23 S. C. 297 (1885); *Hopkins v. Whitesides*, 1 Head (Tenn.), 31; *Bank of*

England the rule has not been applied to insolvent or dissolved moneyed corporations.

§ 639. Where corporate assets are placed in the hands of a corporate officer, or other person, for distribution, a stockholder may file a bill in equity for his part, but in such a suit the corporation is a necessary party.¹ The remedy in such a case is always in equity, and not at law.² The stockholders may insist on the Statute of Limitations as a bar to the claim of corporate creditors upon the assets.³ The rights of the stockholders in the assets upon a dissolution depend upon the law of the country creating the corporation.⁴ And these rights cannot be taken from the stockholders by an act repealing the charter.⁵ But in one case it is held that assets ought to be distributed in proportion as the subscriptions to the stock have been paid.⁶ And this is the rule by statute in New York, upon the voluntary dissolution of a corporation.⁷ Debts due from the stockholder to the corporation are in any event, as of course, to be deducted from his interest in the assets.⁸ And an assignment or transfer of stock by a stockholder, after the dissolution of the corporation, is merely an equitable assignment of his interest in the assets of the concern, as it may appear upon the settlement.⁹

Mississippi v. Duncan, 56 Miss. 166 (1878); *Coulter v. Robertson*, 24 Id. 278; *Acklin v. Paschal*, 48 Texas, 147 (1877).

¹ *Young v. Moses*, 53 Ga. 628 (1875).

² *Brown v. Adams*, 5 Biss. 181 (1870). *Cf. Pacific R. R. Co. v. Cutting*, 27 Fed. Rep. 638 (1886).

³ *Johnston v. Talley*, 60 Ga. 540 (1878). *Cf. Traer v. Clews*, 115 U. S. 528 (1885).

⁴ *Hamilton v. Accessory Transit Co.*, 26 Barb. 46 (1857).

⁵ *Lothrop v. Stedman*, 13 Blatchf. 134 (1875).

⁶ *Krebs v. Carlisle Bank*, 2 Wall. (C. C.) 33 (1850).

⁷ 3 Rev. Stat., chap. XVIII, art. 3, § 83.

⁸ *James v. Woodruff*, 10 Paige, 541 (1844); *Purton v. New Orleans, &c. R. R. Co.*, 3 La. Ann. 19 (1848).

⁹ *James v. Woodruff*, 10 Paige, 541 (1844); s. c. affirmed, 2 Denio, 574 (1845); *Chappell's Case*, L. R. 6 Chan. 902 (1871); *Bank of Commerce's Appeal*, 73 Penn. St. 59 (1873). See *Callanan v. Edwards*, 32 N. Y. 483 (1865); *Sewall v. Chamberlain*, 16 Gray, 581.

PART IV.

STOCKHOLDERS' WRONGS AND REMEDIES AGAINST DIRECTORS, MAJORITY OF STOCKHOLDERS, AND OTHERS, FOR BREACH OF TRUST, &c.

CHAPTER XXXIX.

FRAUDULENT ACTS OF DIRECTORS, MAJORITY OF STOCKHOLDERS, AND THIRD PERSONS.

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A.—THE OCCASION, SCOPE, AND PURPOSE OF THE SUBJECT HEREIN.

§ 640. *The cause and occasion of this subject.*—Perhaps the most striking feature of the era of modern industrial develop-

ment is the growth, wealth, and power of corporations. They have dug the canals, built the railways, established the factories, carried the ocean commerce, and assumed control of the industries of Europe as well as of America. They have absorbed a large part of the surplus wealth of the world, and have accumulated or distributed enormous gains and profits. But these gains and profits have not always been honestly preserved and administered for the benefit of those who are entitled thereto—the stockholders of the company. Corporations, with their vast capital stock, their great income, their rapidly changing personal property, and their large purchases and sales, have proved to be a temptation which corporate officers are too often unable to withstand. These companies have been found to be efficient instruments of fraud, speculation, plunder, and illegal gain. In these latter days the robbery and spoliation of corporations and stockholders by the corporate directors and managers, have been systematized into well-known methods of proceeding, and the carrying out of such plans has become a profession and an accomplishment. The skill, audacity, experience, and talent of the highest order of administrative ability have reduced to a certainty the methods of diverting the profits, capital, and even the existence of the corporation itself, to the enrichment of the corporate managers and their co-conspirators. Corporations become insolvent and stockholders lose their investments, while individuals become millionaires. Illegitimate gains are secured and enormous fortunes are amassed by the few at the expense of the defrauded, but generally helpless, stockholders.

The expense, difficulty, and delays of litigation; the power, wealth, and unscrupulousness of the guilty parties; the secrecy, skill, and evasive nature of their methods; and the fact that the results of even a successful suit belong to the corporation, and not to the stockholders who sue, all combine to baffle investigation and exposure, to discourage the stockholders, and to encourage and protect the parties guilty of the wrong.

§ 641. In England, ever since the year 1720, when the "South Sea Bubble" exploded, and unsettled the finances of the Kingdom, there has been a constant recurrence of "bubble companies" and dishonest promoters. The English reports are filled with cases of frauds of corporate directors, corporate agents,

and corporate organizers. A system of jurisprudence has grown up from these cases. This system, however, is as yet in a formative state, and there is no branch of the law more complicated, difficult, and full of pitfalls for the court, practitioner, and client, than that growing out of the frauds of corporate directors.

§ 642. In America, the cases involving a breach of trust by the directors arise generally out of the management of corporations, and not in their formation. These cases frequently involve colossal transactions, and exhibit a scope, grasp, and ability for railway management and manipulation that excite the stockholder's admiration fully as much as his indignation. It is a curious fact that the American talent for organization, executive management, and the invention and adoption of means to ends, a characteristic talent that formerly was engrossed in the political affairs of the nation, is now very largely engaged in the development and management of the American railroads. With commendable energy, enterprise, daring, and sagacity, the American railway has been built, improved, consolidated, and perfected, frequently far in advance of even the remarkable growth of the country itself. For the most part this work has been done honestly, efficiently, and creditably. But not always has this been the case. The ingenuity and fruitful cunning of adroit, experienced, and unscrupulous talent have plundered and robbed the corporations and the stockholders, and have brought reproach on the management of the American railway. Great fortunes have been accumulated by "wrecking" great corporations. Railroads which were capable of earning a fair return upon the capital invested, have been rendered insolvent by the fraudulent management and illegal gains of the corporate officers. The plans, devices, and methods of accomplishing this result have been systematized and elaborated to a degree equal to the great resources and fertility of mind employed in their execution. It is the purpose of this part of this work to explain, so far as is possible, the methods of those frauds, and to point out the remedy for the wrong.

§ 643. *The three classes of stockholders' wrongs herein.*—Stockholders' wrongs, arising from a breach of trust by directors, a majority of the stockholders, or third persons, are clearly divisible into three classes. They are, first, fraudulent acts; second,

ultra vires acts; third, negligence of corporate directors. There is another class of grievances, that of internal dissensions in the corporation, and dissatisfaction with its policy and acts. All these, however, are *intra vires* of the directors or majority of the stockholders. The law gives no remedy for these dissensions, since the stockholder has the corporate elections as a remedy, and since the majority are to rule, so long as they do so without fraud and within the powers of the corporation.

§ 644. *The corporation is ordinarily the party to remedy these wrongs.*—These frauds, *ultra vires* acts, and acts of negligence, are injuries to the corporation, and the corporation is ordinarily the party to bring suit to rectify them. The frauds, *ultra vires* acts, and negligence of directors, do not affect the stockholder directly, but they affect the stockholders indirectly by decreasing the corporate assets, and thereby affecting the value and privileges of the stock. Accordingly, it is the duty and right of the corporation to bring suit to remedy these wrongs, just as it is the duty and right of the corporation to bring suit to remedy an ordinary trespass, conversion, or fraud, whereby third parties injure the corporate property and interests. That a corporation may bring suit to remedy the frauds, *ultra vires* acts, or negligence of its trustees or directors, was the decision of Lord Chancellor Hardwicke, in 1742, in the case of *The Charitable Corporation against Sutton*.¹

§ 645. *But the corporation failing to do so, a stockholder may bring the action.*—During the next hundred years, however, corporations having a capital stock and stockholders came into existence and rose into prominence. The large capital and great profits of many of these corporations led to frequent frauds, breaches of trust, and illegal acts on the part of the directors. It was the duty of the corporation to bring suit to remedy these wrongs. But it gradually became apparent that frequently the corporation was helpless, and unable to institute the suit. It was found, where the guilty parties themselves controlled the directors and also a majority of the stock, that the corporation was in their

¹ 2 Atk. 400, the court saying: "Nor will I ever determine that a court of equity cannot lay hold of every breach of trust, let the person be guilty of it either in a private or public capacity."

See also, to the same effect, *Attorney-General v. Foundling Hospital*, 4 Bro. Ch. Rep. 165 (1793); *Attorney-General v. Wilson*, 1 Cr. & Ph. 1 (1840).

power, was unable to institute suit, and that the minority of the stockholders were being defrauded of their rights, and were without remedy; and it became apparent that there was a legal wrong which had no legal remedy. The time had come when the minority of the stockholders of a defrauded corporation, the corporation itself being controlled by the guilty parties, must be given a standing in court for the purpose of taking up the cause of the corporation, and in its name and stead bringing the guilty parties to an account. Accordingly, in 1843, in the leading case of *Foss v. Harbottle*,¹ a stockholder brought suit in the name of himself and other defrauded stockholders, and for the benefit of the corporation, against the directors, for a breach of their duty to the corporation. This case was decided against the complaining stockholders on the ground that the complainant did not prove that the corporation itself was under the control of the guilty parties, and that it was unable to institute the suit. The court, however, broadly intimated that a case *might* arise when a suit, instituted by the defrauded stockholders, would be entertained by the court, and redress given. Acting upon this suggestion, and impelled by the utter inadequacy of suits instituted by the corporation, defrauded stockholders continued to institute these suits and to urge the courts of equity to grant relief.² These efforts were unsuccessful in clearly establishing the rights of stockholders herein until the great cases of *Atwood* against *Merryweather*, in England, in 1867,³ and of *Dodge v. Woolsey*, in this country, in 1855.⁴ These two great and leading cases have firmly established

¹ 2 Hare, 461.

² *Mozley v. Alston*, 1 Phil. Ch. 790 (1847), where the court said there is "no reason assigned why the corporation does not put itself in motion to seek a remedy." *Lord v. Governor, &c., of Copper Mines*, 11 Phil. Ch. 745 (1848), where the court refused relief "because the acts were capable of confirmation" by the majority. In the case *Gray v. Lewis*, L. R. 8 Ch. 1035, 1050 (1873), the court said that the preceding cases "have always been considered as settling the law of this court, that where there is a corporate body capable of filing a bill for itself to recover property either from its directors or officers, or from any other person, that corporate body is the proper plaintiff, and the only proper plaintiff, . . . to which, as I understand, the only excep-

tion is where the corporate body has got into the hands of directors and of the majority, which directors and majority are using their power for the purpose of doing something fraudulent against the minority, who are overwhelmed by them." See also *MacDougall v. Gardiner*, L. R. 1 Ch. D. 13 (1875), in regard to the principle of law decided by these cases.

³ L. R. 5 Eq. 464.

⁴ 18 How. 331. The case of *Hawes v. Oakland*, 104 U. S. 450 (1881), is, perhaps, of greater importance than even *Dodge v. Woolsey*, and may take the place of the latter. In *Hawes v. Oakland*, Mr. Justice Miller delivered a masterly opinion, in the course of which he said: "That the vast and increasing proportion of the active business of modern life which is done by corporations should call into exercise

the law for both England and America, that where corporate directors have committed a breach of trust, either by their frauds, *ultra vires* acts, or negligence, and the corporation is unable or unwilling to institute suit to remedy the wrong, a single stockholder may institute that suit, suing on behalf of himself and other stockholders, and for the benefit of the corporation, to bring about a redress of the wrong done directly to the corporation and indirectly to all the stockholders.¹ The rule, as formu-

the beneficent powers and flexible methods of courts of equity, is neither to be wondered at nor regretted; and this is especially true of controversies growing out of the relations between the stockholder and the corporation of which he is a member. The exercise of this power in protecting the stockholder against the fraud of the governing body of directors or trustees, and in preventing their exercise, in the name of the corporation, of powers which are outside of their charters or articles of association, has been frequent, and is most beneficial, and is undisputed." In regard to the doctrine laid down in *Dodge v. Woolsey*, the learned justice says: "We understand that doctrine to be that to enable a stockholder in a corporation to sustain, in a court of equity in his own name, a suit founded on a right of action existing in the corporation itself, and in which the corporation itself is the appropriate plaintiff, there must exist as the foundation of the suit some action or threatened action of the managing board of directors or trustees of the corporation which is beyond the authority conferred on them by their charter or other source of organization; or such a fraudulent transaction completed or contemplated by the acting managers, in connection with some other party, or among themselves, or with other shareholders, as will result in serious injury to the corporation, or to the interests of the other shareholders; or where the board of directors, or a majority of them, are acting for their own interest in a manner destructive of the corporation itself or of the rights of the shareholders; or where the majority of shareholders themselves are oppressively and illegally pursuing a course, in the name of the corporation, which is in violation of the rights of the other shareholders, and which can only be restrained by the aid of a court of equity. Possibly other cases may arise

in which, to prevent irremediable injury or a total failure of justice, the court would be justified in exercising its powers; but the foregoing may be regarded as an outline of the principles which govern this class of cases."

¹ In *Dodge v. Woolsey*, *supra*, the court said: "It is now no longer doubted, either in England or the United States, that courts of equity, in both, have a jurisdiction over corporations at the instance of one or more of their members, to apply preventive remedies by injunction, to restrain those who administer them from doing acts which would amount to a violation of charters, or to prevent any misapplication of their capitals or profits, which might result in lessening the dividends of stockholders, or the value of their shares, as either may be protected by the franchises of a corporation if the acts intended to be done create what is in the law denominated a breach of trust. And the jurisdiction extends to inquire into, and to enjoin, as the case may require that to be done, any proceedings by individuals, in whatever character they may profess to act, if the subject of complaint is an imputed violation of a corporate franchise, or the denial of a right growing out of it, for which there is not an adequate remedy at law." In *Atwood v. Merryweather*, *supra*, the court said: "If I were to hold that no bill could be filed by shareholders to get rid of the transaction, on the ground of the doctrine of *Foss v. Harbottle*, it would be simply impossible to set aside a fraud committed by a director under such circumstances, as the director obtaining so many shares by fraud would be able to outvote everybody else." It is to be noticed that long prior to these cases it had been held by the courts in various cases that a stockholder's action herein would lie, but the principle was not clearly established until the foregoing decisions were made.

lated and enounced therein, has been repeated, applied, explained, and extended, by subsequent cases and by text-books, until a system of jurisprudence may be said to be based thereon. That system is the subject of the present fourth part of this work.¹

§ 646. *The facts and conditions which allow and sustain a stockholder's suit herein.*—Before a stockholder can sustain a suit to remedy the frauds, *ultra vires* acts, or negligence of directors, he should be certain that three distinct facts or conditions exist in his favor. These are, first, that the acts complained of are such as amount to a breach of trust, and such as neither a majority of the directors, nor of the stockholders, can ratify or condone;² second, that the complaining stockholder himself is free from laches, acquiescence, or ratification of the acts to remedy which the suit is brought;³ third, that the corporation has

Thus, in *New York*, as early as 1832, in the case of *Robinson v. Smith*, 3 Paige, 222, the remedy was declared to exist.

¹ Prof. Pomeroy, in his learned work on *Equity Jurisprudence*, § 1094, clearly states the general rule herein as follows: "In general, where the directors or officers, or some of them, cause a loss of corporate property by negligence, or culpable lack of prudence, or failure to exercise their functions, or fraudulently misappropriate the corporate property in any manner, whether for their own benefit or for the benefit of third persons, or obtain any undue advantage, benefit, or profit for themselves by contract, purchase, sale, or other dealings under color of their official functions, or misuse the franchises, or violate the rules established by the charter or the by-laws for their management of the corporate affairs; or in any other similar manner commit a breach of their fiduciary obligations towards the corporation, so that it sustains an injury or loss, and a liability devolves upon themselves, then the corporation is the party which must, as the plaintiff, institute an equitable suit for relief against the wrong-doers; the trust relation between itself, as the *cestui que trust*, and the defaulting directors or officers, as trustees, has been violated, and as in all like cases the *cestui que trust* is primarily the only party to sue for redress. As a general rule, courts of equity will not interfere with the internal management of corporations by means of suits brought by stockholders against directors, officers, or other stockholders.

In cases belonging to this class, therefore, whatever be the nature of the particular wrong, whether intentional and fraudulent, or resulting from negligence or want of reasonable prudence, and whatever be the indirect loss occasioned to individual stockholders, no equitable suit for relief against the wrong-doing directors or officers can be maintained by a stockholder suing representatively on behalf of all others similarly situated, unless the special condition of circumstances exists, to be described in the next following paragraph, namely, that the corporation either actually or virtually refuses to prosecute. Even if the stockholder alleges that the value of his own stock has been depreciated by the defendants' acts, or that he has sustained other special damage, he is not thereby entitled to maintain the suit." In the case of *Mason v. Harris*, L. R. 11 Ch. D. 97 (1879), the court said: "As a general rule, the company must sue in respect of a claim of this nature; but general rules have their exceptions, and one exception to the rule requiring the company to be plaintiff is that where a fraud is committed by persons who can command a majority of votes, the minority can sue. The reason is plain, as, unless such an exception were allowed, it would be in the power of a majority to defraud the minority with impunity."

² This subject is treated in the remainder of this chapter, and in Chapter XL.

³ See Chapter XLI.

been requested and has neglected or refused to institute the suit ; that the suit is instituted by *bona fide* stockholders as complainants, and that the corporation and the guilty parties and other proper parties have been made defendants.¹

B.—FRAUDS OF CORPORATE DIRECTORS, OF A MAJORITY OF THE STOCKHOLDERS, OR OF THIRD PERSONS, TO REMEDY WHICH A STOCKHOLDER MAY BRING SUIT.

§ 647. *Different methods of perpetrating these frauds.*—The various ways in which stockholders are generally defrauded out of their legal rights in a corporation are described in subsequent sections of this chapter. These, however, are the older, and more easily remedied wrongs. The principles of law governing them are known to those who contemplate such frauds. Consequently, new plans and methods of circumventing the law are being constantly devised. There is a continual contest between the courts in branding certain acts as frauds, and the unscrupulous corporate officers in forming new and unknown methods of defrauding the corporation and stockholders. Some of these devices vary little from the older ones, but others are due to the misdirected talent of modern times exclusively. Thus, a frequent fraud is perpetrated in that dividends are withheld, or unduly increased, in order that the corporate managers may cause fluctuations in the price of the stock, and enrich themselves thereby. They exist also when the corporate statements of its condition and business are garbled and arranged so as to mislead the investing public. A favorite modern device is the purchase, by corporate officers, of the stock and bonds of another corporation, and then a consolidation of the two corporations, to the ruin of the former and the enrichment of the holders of the stock and bonds of the latter. Still another method is the diversion of traffic from a corporation, or a use of its income for improvements, whereby its dividends are cut off, until the managers have purchased the stock and bonds at a price far below the real value. These various frauds, and many others which might be enumerated, are discovered and exposed only by great difficulty, and generally only at great expense and delay. The courts of equity are ready and reliable in remedying the wrong, in case the fraud

¹ See Chapter XLII.

can be proved. But in the fact that the proof is concealed or destroyed, and generally beyond the reach of the defrauded stockholder, lies the safety of the guilty parties. The law, however, is clear as to the fraudulent character of many acts specified herein.

§ 648. *Directors as trustees.*—It is frequently said, both in the cases and in the text-books, that the directors of a corporation are practically trustees with the whole body of the stockholders as *cestuis que trustent*. This principle of law has been useful as a method of ascertaining what acts of directors constitute a fraud, and what remedies may be applied. These fraudulent acts and remedies have, however, now been quite accurately defined and ascertained, and it is doubtful whether the law governing trusts is broad enough to circumvent the ingenious plans and schemes of corporate directors to defraud the corporation and stockholders. It is believed that a better and much safer reliance can be placed in the principle of law and equity, that for every wrong there is a remedy. There will be much doubt, confusion, inconsistency, and difficulty in working out the questions which will arise herein, but there can be no doubt of the result, if courts of equity are allowed the same freedom, fearlessness, and power of searching and circumventing all frauds as characterized the origin of such courts.¹

§ 649. *Director or other corporate officer interested in construction company.*—The law is well settled that a director cannot become a contractor with the corporation, nor can he have any personal and pecuniary interest in a contract between the company, of which he is a director, and a third person.² The director cannot be interested in the construction company at the time the contract is made, nor subsequently, and it is immaterial that the contract was fair, or even to the advantage of the corporation. The corporation upon discovering the fact that the direc-

¹ That directors occupy the position of trustees towards the stockholders, see *European, &c. Ry. Co. v. Poor*, 59 Me. 277 (1871); *Hoyle v. Plattsburgh, &c. R. R. Co.*, 54 N. Y. 314; *Koehler v. Black, &c. Co.*, 2 Black, 715. See also *Green's Brice's Ultra Vires*, 2d ed., p. 478, citing many cases. Cf. *Smith v. Anderson*, L. R. 12, Ch. D. 247.

² *Port v. Russell*, 36 Ind. 60 (1871), where an injunction was granted against the payment by a plank road company of

money to a construction company of which a director of the former was a member. The court said that the three leading American cases on the subject of frauds by directors, are *Michaud v. Girod*, 4 How. 503; *Cumberland Coal Co. v. Sherman*, 30 Barb. 553, and *Id.* 20 Md. 117; and *Hoffman Steam Coal Co. v. Cumberland Coal Co.*, 16 Md. 456, and in England, the case *Aberdeen Ry. Co. v. Blaikie*, 1 Macq. 461.

tor is interested in the construction company, may compel him to pay over to the corporation all profits that he has derived from the construction contract.¹ If the company contracting with the corporation secretly gives to the contracting agent of the latter a sub-contract for the construction work, the corporation may re-

¹ Gilman, C. & S. R. R. Co. v. Kelly, 77 Ill. 426 (1875), where the court said "that no director could rightfully become a member of the improvement company, with whom the railroad company had a contract to furnish the means with which to build the road, with a view to share in the profits, and that if any gains should be realized in the enterprise, they would belong to the railroad company, upon the equitable principle which forbids the trustee, or person acting in a fiduciary capacity, from speculating out of the subject of the trust. . . . The inquiry is not whether the contract the trustee has made is the best that could have been made for the *cestui que trust*, or whether it is fraudulent in fact. So strictly is this principle adhered to, that no question is allowed to be raised as to fairness of the contract. The principle has a broader scope. The law has absolutely inhibited the agent or trustee from placing himself in a position where his own private interests would naturally tend to make him neglectful of his obligations to his principal, or where his position would afford him an opportunity to speculate in the trust property. Accordingly, it is not indispensable there should be actual injury before the act of the trustee will be declared void, as being interdicted by the policy of the law. The *cestui que trust* has his election to ratify the act of the trustee, and insist upon all the advantages of it, or disaffirm it *in toto*, as shall be most to his interest."

See also Bayliss v. Lafayette, M. & B. R. R. Co., 8 Biss. 193 (1878); Paine v. Lake Erie, &c. R. R. Co., 31 Ind. 283 (1869); Flint, &c. Ry. Co. v. Dewey, 14 Mich. 477 (1866), where a director had become interested in the construction work, after the contract had been given. The court said: "The principle of law applicable to such a contract renders it immaterial under the circumstances of this case, whether there has been any fraud in fact, or any injury to the company. Fidelity in the agent is what is aimed at, and as a means of securing it, the law will not permit the agent to place himself in a situation in which he may

be tempted by his own private interest to disregard that of his principal." To same effect see Thomas v. Brownville, &c. R. R. Co. 109 U.S. 522 (1883), where, however, it is held that bonds issued to a construction company in which a director is interested cannot be altogether repudiated, but are valid to the extent of the actual value of work done. See also Ryan v. Leavenworth, &c. Ry. Co., 21 Kan. 365 (1879), holding also that a stockholder in a corporation which is a stockholder in the defrauded corporation may sue to remedy the wrong to the latter. European, &c. Ry. Co. v. Poor, 59 Me. 277 (1871), where the court said: "If a director be a party to a contract entered into with himself, his duty as an officer is in conflict with his interests as an individual. This equally so, whether he enters into the contract in its inception or subsequently acquires an interest in it. . . . It is not in that particular instance that the sale or the purchase may not be reasonable, but to avoid temptation, the agent to sell is disqualified from purchasing, and the agent to purchase from selling." See also Risley v. Indianapolis, &c. R. R. Co., 62 N. Y. 240, 248 (1875), where the court said: "The relation which Griggs [president and director] bore to the company, no doubt, placed it in the power of the company to insist that whatever advantages he obtained under the contract assigned to him should be held for the benefit of the company, and that he should account to it for any profit he might make. But at the same time the company had the right, inasmuch as he assumed to act for himself, to hold him to the contract and to refuse to indemnify him against any loss he might sustain by its performance. It was in their power to treat him as contractor if it was to their interest to do so; the disability was upon him, not upon the company; they had the option to treat his dealing as upon their account and at his own risk. . . . The right to insist upon the fiduciary relation which Griggs bore to the company was one existing between the company and him, was one which the company could enforce or waive, as its interests might dictate."

scind the whole contract and recover back the money it has paid out thereon.¹ Nor is a contract valid and enforceable against the corporation where the parties contracting with the corporation have given to the directors of the corporation a secret interest in the profits of the contract.² The circumstances may be such, however, as will vary this rule. Thus, where the director was a surety for the contractor, and the latter failed, the former, who finished the construction work under compulsion by the company, may set up its acquiescence as a bar to its suit to recover from him the profits of the transaction.³ So also where a director pur-

¹ "I take it, according to my view of the law of this court, to be clear that any surreptitious dealing between one principal and the agent of the other principal, is a fraud on such other principal cognizable in this court." *Panama, &c. Tel. Co. v. India Rubber, &c. Tel. Works Co.*, 32 L. T. N. S. 517 (1875). In this case the secret sub-contractor was the agent and engineer of the corporation. He received a commission for his work, and the work was to be accepted subject to his approval.

The case of *Currier v. N. Y., West Shore, &c. R. R. Co.*, 35 Hun, 355 (1885), goes still farther and holds that a stockholder may compel the contractors to disgorge when they obtained the contract with the corporation through their associates or hirelings being made directors. The court said: "If it was the fact that those defendants did control the actions of the railroad company, either through their own acts or those of their associates, as directors thereof, it is plain that since they also controlled the construction company they were simply contracting with themselves, and that the railroad company was helpless in their hands. It requires no argument to demonstrate that a contract made under such circumstances was presumptively fraudulent (citing cases), and that the railroad company might, at its election, treat it as void and repudiate it." (Citing cases.)

² Thus, in *Wardell v. R. R. Co.*, 103 U. S. 651 (1880), under such circumstances the court said: "It is among the rudiments of the law that the same person cannot act for himself and at the same time, with respect to the same matter, as the agent of another whose interests are conflicting. Thus, a person cannot be a purchaser of property and at the same time the agent of the vendor. The

two positions impose different obligations, and their union would at once raise a conflict between interest and duty; and, 'constituted as humanity is, in the majority of cases duty would be overborne in the struggle.' *Marsh v. Whitmore*, 21 Wall. 178, 188. The law, therefore, will always condemn the transactions of a party on his own behalf when, in respect to the matter concerned, he is the agent of others, and will relieve against them whenever their enforcement is seasonably resisted. Directors of corporations, and all persons who stand in a fiduciary relation to other parties, and are clothed with power to act for them, are subject to this rule; they are not permitted to occupy a position which will conflict with the interest of parties they represent and are bound to protect. They cannot, as agents or trustees, enter into or authorize contracts on behalf of those for whom they are appointed to act, and then personally participate in the benefits. Hence, all arrangements by directors of a railroad company, to secure an undue advantage to themselves at its expense, by the formation of a new company as an auxiliary to the original one, with an understanding that they or some of them, shall take stock in it and then that valuable contracts shall be given to it, in the profits of which they, as stockholders in the new company, are to share, are so many unlawful devices to enrich themselves to the detriment of the stockholders and creditors of the original company, and will be condemned whenever brought before the courts for consideration."

³ *Kelley v. Newburyport Horse R. R. Co.*, 141 Mass. 496 (1886), the court saying: "As a general rule, a contract between a corporation and its directors is not absolutely void, but voidable at the election of the corporation. Such a con-

chased an interest in the construction contract after it had been entered into, but sold that interest before any work was done thereunder, the illegality of his connection with the construction company cannot affect the legality of his sale of that interest.¹

✕ § 650. *Secret gifts to directors from persons contracting with the corporation.*—It is a well established principle of law that a director commits a breach of trust in accepting a gift or secret pay from a person who is contracting or has contracted with the corporation, and that the corporation may compel the director to turn over to it all the money or property so received by him. In England these cases generally arise out of gifts of qualification shares given by promoters of the company to the directors who accept office in consequence of such gifts. The corporation may, in such a case, compel the director to pay to it the highest price reached by such stock, between the time when the gift was made and the time when it was discovered.² In this country, these gifts are generally of a different character. Thus, an agreement of a third person to pay a certain sum to a director

tract does not necessarily require any independent and substantive act of ratification, but it may become finally established as a valid contract by acquiescence."

¹ *Barnes v. Brown*, 80 N. Y. 527 (1880).

² *Pearson's Case*, 25 W. R. 618 (1877), aff'g L. R. 4 Ch. D. 222; s. c., L. R. 5 Ch. D. 336 (1877), the court saying: was "Whether the purchase was or not an advantageous one for the company . . . is a question wholly immaterial for us to consider; he cannot, in the fiduciary position he occupied, retain for himself any benefit or advantage that he obtained under such circumstances." *Ormerod's Case*, 25 W. R. 765 (1875), where the director was elected and the gift received after the contract was made. The court said: "If it is lawful that a man may be bought as a director, it must be decided by some one else. I never will decide it." *Weston's Case*, L. R. 10 Ch. D. 579 (1879), where the director was held liable for the full price of the stock less what he paid the promoter therefor. *Clarke's Case*, 37 L. T. N. S. 222 (1877), where the articles of association allowed the gift, but were held to be fraudulent. *McKay's Case*, L. R. 2 Ch. D. 1 (1875),

where the secretary of the corporation was compelled to pay over. *Hay's Case*, L. R. 10 Ch. 593 (1875), where the court said: "No agent can in the course of his agency derive any benefit whatever without the sanction or knowledge of his principal." *Re Englefield Colliery Co.*, L. R. 8 Ch. D. 388 (1877); *Emma Silver M. Co. v. Lewis*, L. R. 4 C. P. D. 396 (1879), where the mining experts of the corporation were compelled to disgorge. *In re Carriage, &c. Assoc.*, L. R. 27 Ch. D. 322 (1884); *Re Drum Slate, &c. Co.*, 53 L. T. 250 (1885), where the promoters gave money to the directors. See also 55 L. J. Ch. 36 (1886); *Madrid Bk. v. Pelly*, L. R. 7 Eq. 442 (1869), where the directors were held to be liable for the money received by them, but for no more. *Nant-y-Glo, &c. Co. v. Grave*, L. R. 12 Ch. D. 738 (1878), holding that the corporation may sue herein, the same as a liquidator. See also *York v. North Midland Ry. Co.*, 16 Beav. 485; *Hunt's Case*, 37 L. J. (Ch.) 278; *Liquidators, &c. v. Coleman*, L. R. 6 H. L. 189; *Benson v. Heathorn*, 1 Young & Coll. 326; *Pelly's Case*, L. R. 21 Ch. D. 492; *Hichens v. Congreve*, 1 R. & M. 150; *Bk. of London v. Tyrrell*, 10 H. L. 26.

if a certain location of a railroad is adopted, or an agreement to allow him to participate in the profits derived from such location, is not an enforceable contract.¹ So also where a director receives a commission from one who obtains a loan from the corporation through the director's influence, the latter may be compelled to pay over the commission to the corporation.² A similar rule was applied where a director of an insolvent insurance company, accepted a secret gift for reinsuring the company's risks in a certain other insurance company.³ And, in general, whenever an agent of the corporation accepts a gift or participates in the profits of a contract with the corporation, the corporation is entitled to the gifts or profits, and a stockholder may bring the suit to compel the agent to pay over.⁴ Frequently gifts are made to directors of watered stock from those to whom it has been issued for property. In such a case the director is liable to the corporation, not for the par value of the stock so received, but its actual value.⁵

¹ *Bestor v. Wathen*, 60 Ill. 138 (1871); *Linder v. Carpenter*, 62 Ill. 309 (1872); *Fuller v. Dame*, 18 Pick. 473 (1836), holding that a promissory note given therefor is void. See also *Union Pac. R. R. Co. v. Durant*, 1 Cent. L. J. 582; *Pac. R. R. Co. v. Seeley*, 45 Mo. 212; *Berryman v. Trustees, &c.*, 14 Bush (Ky.), 755 (1879). In the case *Cook v. Sherman*, 20 Fed. Rep. 167 (1882), the court refused to enforce specifically a contract whereby corporate officers agreed to purchase lands, the purpose of all the parties being to influence thereby the location of the railroad. The court said: "Such a contract by officers of a railroad corporation is contrary to public policy, and one which will not be enforced or made the basis of any relief in a court of equity. The directors of such a corporation are *quasi* public officers. They occupy a position of trust and act in a fiduciary capacity. They represent, not themselves, but the stockholders. They are, in all their official actions, to consider, not their private interest, but that of the stockholders whose property they manage and control. If, as in this case, they are directors of a railway company, with power to locate and construct a public highway, they owe a duty to the public as well as to the stockholders, and are therefore doubly bound to abstain from entering into any scheme to pervert their trusts to their private gain.

The law does not permit these officials to subject themselves to any temptation to serve their own interests in preference to the interests of the stockholders and of the public."

² *Farmers & M. Bk. v. Downey*, 58 Cal. 466 (1879); *Imperial, &c. Assn. v. Coleman*, L. R. 6 H. L. 189 (1873).

³ *Bent v. Priest*, 1 West. Rep. 749 (Mo. 1885). See also *Gaskell v. Chambers*, 28 Beav. 360.

⁴ *Bank of London v. Tyrrell*, 5 Jur. N. S. 924 (1859), where a solicitor of the corporation was compelled to pay over under such circumstances. The court said: "It is not a question about setting aside the transaction, neither is it a question of what is or was the true value of the property; but the question is, whether the agent has not by means of his agency acquired this property for the purpose of making a profit out of it by a resale to his principal, and whether, if he succeeds in his object, he can keep that advantage to himself." *Phosphate Sewage Co. v. Hartmont*, L. R. 5 Ch. D. 399 (1877); *General Ex. Bk. v. Horner*, 39 L. J. (Ch.) 393 (1870), where the manager was paid a large sum in order to obtain his aid to a consolidation scheme.

⁵ *Morrison v. Globe Panorama Co.*, 28 Fed. Rep. 817 (Nov. 1886). See also § 48, *supra*; *Pacific Trust Co. v. Dorsey*, 12 Pac. Rep. 49 (Cal. 1886).

§ 651. *Frauds by promoters on the corporation.*—A promoter is a person who brings about the incorporation and organization of a corporation. He brings together the persons who are interested in the enterprise, aids in procuring subscriptions, and generally is the representative of parties who wish to sell property to the corporation, or to construct its works.¹ A promoter is considered in law as occupying a fiduciary relation towards the corporation. He is an agent of the corporation and his compensation is derived from it, or from the persons who are the principal stockholders of the corporation. The promoter is not allowed to receive and retain a secret profit given to him by the parties with whom the corporation contracts.² Frequently the promoter himself owns or has an interest in the property which is sold to the corporation. In such cases if he openly acknowledges such interest and deals with the company at arm's length the transaction is allowed to stand. But if the promoter conceals his interest in the property sold to the corporation the sale may be set aside, the property returned, and the money recovered back.³ Generally, however, the promoter has previously purchased the

¹ *Emma Silver M. Co. v. Lewis*, L. R. 4 C. P. D. 396 (1879), where Lindley, J., says that the word "promoter" has no very definite meaning. The court said: "As used in connection with companies the term 'promoter' involves the idea of exertion for the purpose of getting up and starting a company (or what is called 'floating' it), and also the idea of some duty towards the company imposed by or arising from the position which the so-called promoter assumes towards it. It is now clearly settled that persons who get up and form a company have duties towards it before it comes into existence." And again, in *Emma, &c. Co. v. Grant*, L. R. 11 Ch. D. 918 (1878), a promoter is defined as "a trustee, agent, or person in a fiduciary position as regards the company, one who has undertaken a duty towards the company of such a character as incapacitates him from making a secret profit at the expense of the company." Lydney, &c. Co. v. Bird, L. R. 31 Ch. D. 328, says: "No doubt a very little will make people promoters of a company, if it can be seen that they were really doing something in the way of speculation for their own interest and not acting merely as agents for others."

² *Emma Silver, &c. Co. v. Grant*, L. R. 11 Ch. D. 918 (1878), where the promoter was compelled to disgorge a gift given to him by the vendors of a mine to the corporation, but he was allowed to retain therefrom his disbursements. It is immaterial that the sale was a fair one. The court said: "He must let his company know what profit he has taken and deal with them, so to say, at arm's length." *Whaley Bridge, &c. Co. v. Green*, L. R. 5 Q. B. D. 109 (1879), holding also that if the vendor has not yet paid the money to the promoter the corporation may recover it from the former. See also *Bagnall v. Carlton*, L. R. 6 Ch. D. 371; *St. Louis, &c. Co. v. Jackson*, 5 Cent. L. J. 317; *Re Murvah, &c. Co.*, 24 W. R. 49 (1875).

³ *New Sombrero P. Co. v. Erlander*, L. R. 5 Ch. D. 73, 103 (1877); *aff'd*, 3 App. Cas. 1218, where the promoters purchased a mine, organized the company, controlled the directors, and sold the property to the corporation at a great advance. *Lindsay Petroleum Co. v. Hurd*, L. R. 6 C. P. D. 221; *Phosphate Sewage Co. v. Hartmont*, L. R. 5 Ch. D. 394 (1877).

property at a price much less than that which the corporation pays him. In such cases he may be compelled to pay over to the corporation his profits in the transaction.¹ The agent of the person who sells to the corporation is not a promoter of the latter. He bears a very different relation towards it from the relation of a promoter—one who acts for the corporation. The agent of the person who deals with the corporation may recover his compensation from that person, but he cannot recover compensation for improperly influencing the agents of the corporation to make the contract.²

§ 652. *Sales of property by corporate officers to the corporation.*—It is well said, in the case of *Michaud v. Girod*,³ that a person cannot legally purchase on his own account that which his duty or trust requires him to sell on account of another, nor purchase on account of another that which he sells on his own account. He is not allowed to unite the two opposite characters of buyer and seller. Especially is this the rule with corporate directors. If they make sales to the corporation they may be compelled to pay over to the corporation the profit realized by such sales⁴ or the corporation may refuse altogether to complete the contract.⁵ Generally the director has purchased the property for

¹ *Simons v. Vulcan Oil, &c. Co.*, 61 Penn. St. 202 (1869), where the promoter misrepresented the price which he gave for the property. This case is quite properly considered as the leading case on this subject and is so presented by Judge Thompson in his learned work on *The Liability of Officers and Agents of Corporations*. See also *Hichens v. Congreve*, 4 Russ. 563 (1828); *In re Hereford, &c. Co.*, L. R. 2 Ch. Div. 621; *Bk. of London v. Tyrrell*, 5 Jur. N. S. 924. *Cf. Gover's Case*, L. R. 1 Ch. D. 182. Where the vendor of the property to the corporation realized one price; the promoter received from the corporation a much greater price and retained the difference, *McElhenny's Appeal*, 61 Penn. St. 183 (1869), the court said: "The promoters of such companies, when they buy to form a company and their purchases are taken by the company . . . cannot make profits on these sales." The vendor of the property to the promoter was also implicated herein. See also *Phosphate, &c. Co. v. Hartmont*, *supra*.

² *Lydney, &c. Co. v. Bird*, L. R. 31

Ch. D. 328; *Arkright v. Newbold*, L. R. 17 Ch. D. 301; *Davidson v. Seymour*, 1 Bosw. (N. Y.) 88 (1857), where the court says: "There was secrecy, applications to individuals, a concealed promise of compensation, and utter ignorance and recklessness as to the competency of the party whose cause he was promoting and whose reward he was to receive." *Densmore Oil Co. v. Densmore*, 64 Penn. St. 43.

³ 4 How. 503 (1846).

⁴ *Abbin Street, &c. Co. v. Martin*, 24 W. R. 134 (1875); *Benson v. Heathorn*, 1 Y. & C. (Ch.) 326 (1842); *Dunne v. English*, L. R. 18 Eq. 524 (1874), there having been no full disclosure to and ratification by the corporation.

⁵ *Coleman v. Second Ave. R. R. Co.*, 38 N. Y. 201 (1868); *Metropolitan Ry. Co. v. Manhattan Ry. Co.*, 15 Am. & Eng. R. R. Cas. 1, 74 (N. Y. 1884), *Van Brunt, J.*, saying: "I think, therefore, that the undoubted rule of law in this State is, that every contract entered into by a director with his corporation may be avoided by the corporation within a

the express purpose of selling it to the corporation. When such is the case the company may ratify and confirm the transaction, or it may keep the property and recover from the director the profit realized by him, or the company may repudiate the whole transaction, return the property, and recover back the purchase money.¹ Where, however, the directors sell to the corporation at a profit to themselves, but with a full and fair disclosure thereof, and without participating in the acceptance by the corporation of the property, the transaction cannot be impeached afterwards.² Moreover it is within the power of the majority of the stockholders to ratify and confirm such a transaction where there is no *actual* fraud involved. The fraud is not an *actual* one if the director sold at a fair price and did not use his position to induce the corporation to purchase. Such a sale, however, is always a constructive fraud, and is voidable at the option of a majority of the directors or a majority of the stockholders. There is some difficulty in determining what will constitute a confirmation of such a transaction. If a majority of the directors and of the stockholders, without counting the votes controlled by the director who is interested, favor a confirmation of the transaction, a dissenting stockholder cannot bring suit to set it aside unless he can show the existence of some fraud other than the mere fact that the vendor was a director when he made the sale.³ If, however, a majority of the stockholders, excluding the votes owned directly or indirectly by the guilty parties, are in favor of bringing the directors to an accounting, a single stockholder may file a bill in equity for that purpose. It was on such a state of facts that the great case of *Atwood v. Merryweather* was decided.⁴

reasonable time, irrespective of the merits of the contract itself." In the case of *Great Luxembourg Ry. Co. v. Magnay*, 25 Beav. 586, where the director purchased for the corporation, property secretly owned by himself, the court refused to interfere after the corporation had resold the property without loss. Under this principle of law the court refused to enforce a contract by a director to furnish railway chairs to his corporation. *Aberdeen Ry. Co. v. Blakie*, 1 Macq. 461; and in the case *Flanagan v. Great Western Ry. Co.* L. R. 7 Eq. 116 (1868), the court refused to enforce a corporate agreement to lease property to a director.

¹ *Parker v. Nickerson*, 112 Mass. 195 (1873); *Redmond v. Dickerson*, 9 N. J. Eq. 507 (1853). See also *Getty v. Devlin*, 54 N. Y. 403 (1873); *Brewster v. Hatch*, 10 Abb. N. C. 400 (1881).

² *Chesterfield Colliery Co. v. Black*, 37 L. T. 740; *British Seamless, &c. Co., L. R. 17 Ch. D. 467*; *Imperial, &c. Co. v. Coleman*, L. R. 6 Ch. 568. *Cf. Id.* 6 H. L. 189.

³ *Beatty v. North West, &c. Co.*, 5 Canadian Law Times, 277 (1885); *Foss v. Harbottle*, 2 Hare, 461 (1843).

⁴ L. R. 5 Eq. 464 (1867). See also *Mason v. Harris*, L. R. 11 Ch. D. 97 (1879). *Cf. however, East Paut, &c. Mining Co. v. Merryweather*, 2 H. & M. 254,

§ 653. *Purchases by directors from the corporation.*—One of the most frequent frauds perpetrated upon a corporation and its stockholders, is where one or more of the directors purchase property from the corporation directly or indirectly, or participate in the profits of such a purchase. The law is well settled that a director's purchase of property from the corporation is voidable at the option of the corporation, even though the director paid fully as much as or more than the property is worth. This principle of law was fully established by the cases of Cumberland Coal Company against Sherman¹ and Hoffman Steam Coal Company against Cumberland Coal and Iron Company.²

261, n., where the court says: "As to the management of the company by the board no director is entitled to vote as director in respect of any contract in which he is interested, but the case is different where he acts as one of a whole body of shareholders. The shareholders of one company may have dealings with interests in other companies, and therefore it would be manifestly unfair to prevent an individual shareholder from voting as a shareholder in the affairs of the company. At a general meeting his vote must be held to be good so long as he continues to hold his shares." Prohibition against his voting as director does not prevent his voting as stockholder. On the general principle that a director is not allowed to make a profit out of his position. See also North Eastern Ry. Co. v. Jackson, 19 W. R. 198; Smith v. Anderson, L. R. 15 Ch. D. 247; Parker v. McKenna, L. R. 10 Ch. 118; McKay's Case, L. R. 2 Ch. D. 1; Albion Steel Co. v. Martin, L. R. 1 Ch. D. 585.

¹ 30 Barb. 533 (1859), where the court said that they who assume "the position of directors and trustees, assume also the obligations which the law imposes on such a relation. The stockholders confide to their integrity, to their faithfulness, and to their watchfulness, the protection of their interests. This duty they have assumed, this the law imposes on them, and this those for whom they act have a right to expect. The principals are not present to watch over their own interests; they cannot speak in their own behalf; they must trust to the fidelity of their agents. If they discharge these important duties and trusts faithfully, the law interpose its shield for their protection and defense; if they depart from the line of

their duty and waste, or take themselves, instead of protecting the property and interests confided to them, the law, on the application of those thus wronged or despoiled, promptly steps in to apply the corrective, and restores to the injured what has been lost by the unfaithfulness of the agent. This right of the *cestui que trust* to have the sale vacated and set aside where his trustee is the purchaser, is not impaired or defeated by the circumstances that the trustee purchases for another." The court also said that the purchase by the directors could be ratified only by the unanimous vote of all the stockholders; and that a ratification by a proxy would not bind the stockholder himself.

² 16 Md. 456 (1860), where a minority of the directors purchased part of the corporate property at an undervaluation and then sold it to the Hoffman Company, in which they were large stockholders. The court held that the latter was chargeable with notice of the voidable act. The court said: "Trustees cannot purchase at their own sales, either directly or indirectly, and if they do, such purchase will be set aside on the proper and reasonable application of the parties interested." This rule applies to directors who act "in a fiduciary capacity, which imposes upon them the obligation of obtaining the best terms for the vendor, or which has enabled them to acquire a knowledge of the property." This case and the preceding one grew out of the same transactions. See also Buell v. Buckingham, 16 Iowa, 284 (1864), holding that the purchase is voidable, but not void. It may be avoided, however, without proving any actual fraud on the part of the director or injury to the corporation. It is fraudulent *per se*. See also Jones v. Arkansas

Similar rules prevail in regard to a director's purchases of corporate property at a foreclosure sale thereof. A director may loan money to a corporation, take a mortgage therefor in good faith, and may foreclose the mortgage if the principal or interest is not paid.¹ But at this point the privileges of the director cease. He cannot be a purchaser, either directly or indirectly, at the foreclosure sale. This is the rule whether the foreclosure is instituted by those interested in the corporation or by third parties. If the director purchases at such a foreclosure sale he holds the property as trustee for the benefit of the corporation and the stockholders. Upon being repaid the price he gave therefor, he must make over the property to the corporation.² Thus where a director who

M. & A. Co., 38 Ark. 17 (1881); Haywood v. Lincoln Lumber Co., 26 North West. Rep. 184 (Wis. 1885); Dennis v. Kennedy, 19 Barb. 517 (1864). The passive connivance of a director renders him liable the same as though he participated. Weetjen v. Vibbard, 5 Hun. 265 (1875).

¹ Harts v. Brown, 77 Ill. 226 (1875), the court saying: "We have never heard it questioned that a director or stockholder may trade with, borrow from, or loan money to the company of which he is a member on the same terms and in like manner as other persons. . . . But in doing so he must act fairly and be free from all fraud and oppression; and he in so doing must act for the interest of the company and impose no unfair or unreasonable terms."

But where the corporation is insolvent, it seems that the directors cannot turn in to themselves its property for the purpose of paying a debt due from the corporation to them. Bradley v. Farwell, 1 Holmes, 433 (1874). See also Williams v. Patrons of Husbandry, 5 West. Rep. 105 (Mo. 1886). And a mortgage given when the company is nearly insolvent "requires to be supported by evidence so strong and clear as to remove every reasonable doubt of the fairness and honesty of the transaction." Hope v. Salt Co., 25 W. Va. 789 (1885). Cf. Bassett v. Monte Christo, &c., Co., 15 Nev. 293 (1880). See § 660, *infra*. In West Virginia there is a code provision, Ch. 53, § 52, to the following effect: "No member of the board shall vote on a question in which he is interested otherwise than as a stockholder, or be present at the board while the same is under consideration; but if his retiring from the board

in such case reduce the number present below a quorum, the question may nevertheless be decided by those who remain." In England also this matter is regulated by act of Parliament.

² Harts v. Brown, *supra*, the court saying the directors cannot purchase "any more than they could fix a price on the property and appropriate it to their own use, which the law has never sanctioned with persons occupying the relation they did to the stockholders." To same effect, Hope v. Salt Co., 25 W. Va. 789 (1885), where the director resold the property at three times its cost to himself. See also Jackson v. Ludeling, 21 Wall. 616, 625 (1874), where the directors were part of those who purchased at a foreclosure sale of the corporate property. The court said: "They had no right to enter into or participate in a combination, the object of which was to divest the company of its property and obtain it for themselves at a sacrifice, or at the lowest price possible. They had no right to seek their own profit at the expense of the company, its stockholders, or even its bondholders. Such a course was forbidden by their relation to the company. It was their duty, to the extent of their power, to secure for all those whose interests were in their charge, the highest possible price for the property which could be obtained for it at the sheriff's sale. They could not rightfully place themselves in a position in which their interests became adverse to those of either the stockholders or bondholders. And this rule was peculiarly applicable to these defendants." Also Munson v. Syracuse, &c. R. R. Co., 29 Hun. 76 (1883), where the directors purchased for

practically controlled the board of directors caused all the earnings of the railroad to be used in improving the property, thereby preventing a payment of interest on the corporate indebtedness and bringing about a foreclosure of the mortgage, the director himself having purchased the bonds secured by the mortgage, and having purchased the railroad at the foreclosure sale, the court in an able opinion held that the purchase at the foreclosure sale by the director was voidable. Upon repayment to him of the purchase price, he may be compelled to retransfer the property to the corporation, even though another foreclosure will be the result: Third persons who have purchased the road from him with notice stand in no other position than the director himself.¹ A director cannot purchase corporate property sold under

the purpose of reorganizing the corporation. But in *Twin Lick Oil Co. v. Marbury*, 91 U. S. 587 (1875), where a director loaned money to the corporation, took bonds therefor, and had the bonds secured by a mortgage running to a third person as trustee, and upon a sale by the trustee the director purchased for himself, the court said: "If it be conceded that the contract by which the defendant became the creditor of the company was valid, we see no principle on which the subsequent purchase under the deed of trust is not equally so. The defendant was not here both seller and buyer. A trustee was interposed who made the sale, and who had the usual powers necessary to see that the sale was fairly conducted, and who in this respect was the trustee of the corporation and must be supposed to have been selected by it for the exercise of this power. Defendant was at liberty to bid, subject to those rules of fairness which we have already conceded to belong to his peculiar position; for, if he could not bid, he would have been deprived of the only means which his contract gave him of making his debt out of the security on which he had loaned his money. We think the sale was a fair one. The company was hopelessly involved beside the debt to defendant. The well was exhausted to all appearance. The machinery was of little use for any other purpose, and would not pay transportation. Most of the stockholders who now promote this suit refused to pay assessments on their shares to aid the company. Nothing was left to the defendant but to buy it in, as no one would bid the amount of his debt." The court said,

moreover, that although the corporation might have avoided the director's purchase, yet a long delay in so doing would bar its right. See Chapter XLI. In the recent case of *Munson v. Syracuse, &c. Ry. Co.*, 8 North-east. Rep. 355 (N. Y. Ct. of App. Oct. 1886), where Munson was a director in an insolvent railroad corporation and also a director in a corporation that wished to purchase said railroad, and in behalf of the latter company contracted to purchase the said railroad from the bondholders after the latter should purchase the same at a foreclosure sale, the court refused to enforce the contract and said that the director "stood in the attitude of selling as owner and purchasing as trustee. The law permits no one to act in such inconsistent relations. It does not stop to inquire whether the contract or transaction was fair or unfair. It stops the inquiry when the relation is disclosed, and sets aside the transaction, or refuses to enforce it at the instance of the party whom the fiduciary undertook to represent without undertaking to deal with the question of abstract justice in the particular case. It prevents frauds by making them, as far as may be, impossible, knowing that real motives often elude the most searching inquiry, and it leaves neither to judge nor jury the right to determine upon a consideration of its advantages or disadvantages whether a contract under such circumstances shall stand or fall."

¹ *Covington & Lex. R. R. Co. v. Bowler's Ex'rs*, 9 Bush (Ky.), 570 (1872), the court saying: "There is no doctrine better settled nor more universally recognized than that an agent or trustee can-

execution,¹ nor purchase, either in their own name or the name of another, corporate property sold for the payment of taxes.² The corporation may reclaim the property upon payment to the director of the amount he paid therefor. A similar rule applies where a director allows or brings about a forfeiture of a lease which the company holds as lessee, and then takes a new lease of the same property in his own name.³ The disability of directors to purchase property from the corporation does not restrict their right to subscribe for unissued stock of the corporation.⁴ There is some difficulty in determining whether this disqualification of a corporate officer to purchase property from the corporation extends to officers other than the president and directors. It has been held to affect the treasurer of the corporation,⁵ and also the cashier of a bank.⁶ It has also been intimated that a superintendent of the corporation is under the same disability.⁷

not rightfully place himself in a position exciting in his own bosom a conflict between self-interest and the duty he owes to those for whom he acts. Generally such persons will not be allowed to purchase and make profit out of the estate of those toward whom they occupy a confidential relation." In the case *Kitchen v. St. Louis, &c. Ry. Co.*, 69 Mo. 224 (1878), the court says: "Whatever is sufficient to put a person on inquiry is notice; that is, where a man has sufficient information to lead him to a fact he shall be deemed cognizant of it."

¹ The director "could not become the purchaser of the property of the corporation except subject to its right to elect to disaffirm the sale and demand a resale. As director it was his duty to prevent a sale if possible, and if not then to endeavor to have the property produce the highest price, and in order to the attainment of these objects to use the knowledge he had derived from the confidence reposed in him as director. As purchaser, on the other hand, it was his interest to pay as little as possible, and to use his special knowledge for his own advantage. Actual fraud or actual advantage do not need in such cases to be shown." *Hoyle v. Plattsburg, &c. R. R. Co.*, 54 N. Y. 314 (1873).

² *Smith v. Fagan*, 17 Cal. 178 (1860).

³ *Bengley v. Wheeler*, 45 Mich. 493 (1881); *Smith v. Bank of Victoria*, 41 L. J. (P. C.) 34 (1872). In the latter case

the director reorganized and allowed part of the old stockholders to come in. A dissenting stockholder caused the whole transaction to be set aside.

⁴ *Sims v. Street R. R. Co.*, 37 O. St. 556 (1882). See also § 61. *Cf. Charleston Ins. & Trust Co. v. Sebring*, 4 Rich. Eq. (S. C.) 342 (1853), where the directors purchased from the corporation stock which the corporation had previously issued and had purchased for itself. See also *Parker v. McKenna*, L. R. 10 Ch. 96 (1874), and *York, &c. Ry. Co. v. Hudson*, 16 Beav. 485 (1853), holding that upon an increase of the capital stock the directors have no right to make a secret profit in its disposal.

⁵ *McAllen v. Woodcock*, 60 Mo. 174 (1875), holding that the treasurer's purchase of the corporate property at an execution sale thereof is a purchase for the benefit of the corporation. So also *Parker v. Nickerson*, 112 Mass. 195.

⁶ *First Nat'l Bk. v. Drake*, 1 Am. & Eng. Corp. Cas. 210 (Kan. 1883).

⁷ *Cook v. Berlin Woolen M. Co.* 43 Wis. 433 (1877). In this case the superintendent's purchase was illegal, inasmuch as one of the directors was a secret partner in the purchase. The court said: "A distinction is recognized in the books between corporate officers whose offices are of the essence of the corporation and whose offices are merely ministerial. Courts of equity deal with the former as trustees, with the latter as agents. . . . Where the trustee's sale to a stranger

§ 654. *Reorganization and purchases of corporate property by a majority of the stockholders.*—The term reorganization, as applied to corporations, may be said to be a business arrangement whereby a new corporation is formed and the property of an old corporation is transferred to the new corporation. There are in general three methods in which a reorganization may be effected. The first method is by a foreclosure of a mortgage on the corporate property. Ordinarily a foreclosure proceeding proceeds quietly to a sale of the property. But the large interests involved in a railway foreclosure leads to strenuous opposition thereto. Accordingly it is found to be expedient, during or previous to a railway foreclosure suit, for the parties interested in the property, whether they be the stockholders or bondholders or mere outsiders, to formulate and propose to the bondholders and stockholders a plan of reorganization whereby, after a foreclosure sale, the purchaser of the property will allow the said bondholders, and often also the stockholders, to come into a new company which shall own the property so purchased. It has been found necessary, in most cases, to reorganize on some such plan, in order to quiet the defense to the foreclosure, or to raise the funds required in the reorganization, or to obtain a charter from the State for the reorganized enterprise, or to preserve intact the system of railways, branches, leases, and connections, which give value to the property foreclosed. This method of effecting a reorganization is legal and valid, since it involves an ordinary foreclosure of a mortgage and an agreement of interested parties to purchase at the foreclosure sale. The foreclosure cuts off all rights of the old corporation and stockholders to the property foreclosed, and also the rights of the bondholders whose mortgage is foreclosed.¹ The only rights which any of these parties have,

is colorable only, and made in whole or in part for the use of the trustee, or upon any understanding, express or implied, between the trustee and the purchaser, for any future interest of the trustee in the purchase or in the trust property purchased, a court of equity will deal with the trustee as a direct purchaser from himself, and will avoid his purchase at the suit of his *cestui que trust*." The court said that so long as the contract is executory the director cannot become interested in the property, and "it may be regretted, though too late, that such pur-

chases can ever be upheld." A stockholder may bring suit to set aside the transaction. "Courts of equity have long recognized this right of self-protection in stockholders, and the administration of many corporations in these days tends to show the wisdom and justice of the rule."

¹ Thus where, in order to quiet opposition to a foreclosure, the bondholders offer to the stockholders a plan of reorganization whereby the foreclosure is to proceed, a sale be made, a new corporation formed to take the property, and the

after the foreclosure, are such rights as the plan or contract of reorganization gives them. By this plan generally the old stockholders are allowed to come into the new corporation upon the payment of a fixed sum for each share of stock held by them. The bondholders are generally allowed to exchange the old bonds for new ones in the new corporation, on different terms of interest and times of payment. Plans of reorganization, such as this, are favored by the courts.¹ There must, however, have been no fraud or collusion exerted whereby the property at the sale brings less than its real value. The courts uphold purchases by the reorganization company, for the reason that thereby a better price is obtained for the property than could probably be obtained otherwise. Thus it has been held that a purchase of corporate property by a majority of the stockholders at a foreclosure sale, if made in good faith and without oppression or undue advantage being taken of the minority, is legal and void. It is not constructive fraud. The purchases by a majority of the stockholders may be objected to and set aside only when they are *actually* fraudulent.² The rule, however, is different where the purchaser at the foreclosure sale was a director of the old corporation. Such a purchase is fraudulent as a matter of law, even though made in good faith and a full price paid for the property.³ The corporation or a dissenting stockholder may cause the sale to be set aside, or may claim for the corporation the property itself, upon repayment to the director of the price he paid therefor. It is a rule of law, also, that the trustee of the mortgage itself cannot purchase at the foreclosure, even for the benefit of the bondholders and stockholders.⁴ It is important to mention, in this connection, that

old stockholders to be allowed to come in if they apply within a certain time, and this plan is carried out, a stockholder who had no knowledge of the plan until after the limited time had expired, cannot compel the new corporation to admit him. His remedy, if he has any, is to impeach the foreclosure. *Thornton v. Wabash Ry. Co.*, 81 N. Y. 462 (1880).

¹ "Without such previous organizations and arrangements great sacrifice and loss must attend all such sales. They are, therefore, to be promoted, rather than discouraged by unnecessary and improper exposure of their membership." *Robinson v. Philadelphia, &c. R. R. Co.*, 28 Fed. Rep. 340 (1886). In an action

by a stockholder to set aside a foreclosure sale, which he alleges was collusive and fraudulent, in that the bondholders and part of the stockholders had arranged to have the foreclosure made for the purpose of reorganization, is demurrable unless the consenting stockholders and the trustees in the mortgages are made parties defendant. *Ribon v. R. R. Companies*, 16 Wall. 446 (1872). See also *Harpending v. Munson*, 91 N. Y. 650, with reference to the corporation as a party to the suit.

² See *Carter v. Ford Plate Glass Co.*, 85 Ind. 180 (1882), and see § 662.

³ See § 653, *supra*.

⁴ *Kitchen v. St. Louis, &c. Ry. Co.*,

a collusive foreclosure, whereby the corporate directors who might make a valid defense do not do so, but allow judgment to be taken by default, may be impeached and set aside by a stockholder on the ground of fraud.¹ Sometimes a strict foreclosure of the mortgage has been made, and it has been held where such a foreclosure has been made of a railroad mortgage, that the plan of reorganization as adopted by the majority of the bondholders and confirmed by a charter of incorporation from the legislature, is binding on the minority.²

§ 655. The second method of reorganization may be said to be a reorganization under a mortgage foreclosure sale, as in the preceding method, but under a plan prescribed by statute for letting in the old bondholders and stockholders. It generally is necessary for the purchasers at the foreclosure sale to reorganize under a statute where such a statute exists, since usually under that statute only will the State grant a charter of incorporation to the purchasers.³ Such reorganization statutes exist in several of the States.⁴ Generally the statute prescribes the procedure to be followed in allowing the stockholders of the old corporation to be-

69 Mo. 224 (1878), holding, however, that delay will bar the right of other parties to object.

¹ See § 659, *infra*.

² *Gates v. Boston, &c. R. R. Co.*, 53 Conn. 351; see also, on reorganizations, *Shaw v. R. R. Co.*, 100 U. S. 605 (1879); *Canada Southern Ry. Co. v. Gebhard*, 109 U. S. 527 (1883); *Child v. N. Y. &c. R. R. Co.*, 129 Mass. 170; *Matthews v. Murchison*, 15 Fed. Rep. 691. See *Knapp v. R. R. Co.*, 20 Wall. 117 (1873); *Bliss v. Matteson*, 45 N. Y. 22 (1871), holding that a special agreement with an influential bondholder, giving him an advantage over other similar bondholders, is void. *Railroad Co. v. Howard*, 7 Wall. 392 (1868), holding that an agreement whereby the stockholders receive compensation and allow the foreclosure, is void, since the corporate creditors are entitled to the whole value of the property, which necessarily included the compensation paid to the stockholders.

³ It is clearly established that the purchasers at the foreclosure sale do not succeed to the corporate capacity and franchise of the old corporation. *Metz v. Buffalo, &c. R. R. Co.*, 58 N. Y. 61 (1874); *Wellsborough, &c. P. R. Co. v. Griffin*, 57 Penn. St. 417. See also an

able article on Foreclosure of Railway Mortgages by R. Mason Lisle, in *American Law Review*, Dec., 1886. Cf. *Commonwealth v. Central Passenger Ry. Co.* 52 Penn. St. 506—under a statute. This corporate franchise is to be distinguished from the eminent domain franchise which was exercised by the old corporation. The latter franchises generally pass under the mortgage as authorized by statute. A reorganization under the usual statute has the effect of creating a new corporation. It is not a mere amendment of the old charter. *Marshall v. Western N. C. R. R. Co.*, 92 N. C. 322 (1885).

⁴ The New York statute of 1853 (ch. 502, § 2), whereby within six months after a foreclosure sale of a railroad any or all of the old stockholders might come into the new corporation by paying their proportion of the execution sale price, was repealed by Laws of 1854, ch. 282, and Laws of 1874, ch. 480, the latter being the act "to facilitate the reorganization of railroads sold under mortgages," &c. See *Pratt v. Munson*, 84 N. Y. 582 (1881). The act of 1874, ch. 480, now regulates reorganization incorporations in New York State. For Ohio, see *R. S.* 1880, §§ 3393 *et seq.*

come members of the new corporation. Where such a procedure is prescribed and a newspaper advertisement is made as required by statute, limiting the time within which the old stockholders must apply for admission into the new corporation, a stockholder of the old corporation, who fails to apply within the prescribed time, is barred of all right to come into the new corporation, and a court of equity cannot give him any relief.¹

§ 656. That which may be called a third method of reorganizing a corporation is where the directors or the stockholders turn over the assets of the corporation to a new corporation. This is done in various ways. It may be by a consolidation with another company, or by a sale or lease of the whole corporate property to that other corporation. The validity of such acts as against the dissent of a stockholder has been treated elsewhere.² The validity of such sales of the corporate property is generally determined by ascertaining whether the sale is *ultra vires* or not. Sometimes, however, an element of fraud is involved and will suffice to set aside the transaction. Thus it is illegal and fraudulent for the majority of the stockholders to purchase the property of the corporation at a sale authorized by themselves.³ Such a purchase by the majority may be set aside in the same way and to the same extent that a purchase of corporate property by a director may be set aside.⁴ This is the rule, even though the majority purchase and proceed to a reorganization of the corporation, and offer to allow all the stockholders to become members of the new corporation.⁵ That a purchase by a corporation direc-

¹ *Vatable v. N. Y. &c. R. R. Co.*, 96 N. Y. 49 (1884), the court saying: "It would lead to intolerable inconvenience, confusion and difficulty if the stockholders of the old company could in such a case take their own time to assent to the plan of reorganization, and to assert their right to become members of the new company upon such facts as they would be able to establish in a court of equity." Rev'g 11 Abb. N. C. 133.

² See Chapter XL.

³ See § 662, *infra*. See also *Reilly v. Oglesby*, 25 W. Va. 36 (1884), where the court said: "It is a well-settled principle of equity jurisprudence, that a party holding a fiduciary relation to trust property cannot become the purchaser of

such property, either directly or indirectly; and, if he does, the sale is voidable, and will be set aside at the mere pleasure of the beneficiaries, although such fiduciary may have paid a full price and gained no advantage. . . . A purchase by or for them at a sale ordered by them, acting in the capacity of directors . . . would be voidable and would be set aside at the mere pleasure of any stockholder."

⁴ *Id.*

⁵ *Banks v. Judah*, 8 Conn. 145 (1830), holding, however, that long delay of a dissenting stockholder in bringing suit will bar his remedy. This, perhaps, is the first reorganization case that is to be found in the books. The formation of a

tor at such a sale is voidable is well established.¹ It is also fraudulent and illegal for the majority to dissolve the old corporation, form a new one, and sell the property of the old one to the new corporation at a valuation placed upon the property by the majority themselves.²

§ 657. *Voting salaries or compensation to corporate officers.*—A frequent fraud upon corporations and stockholders is perpetrated by the corporate funds being used to pay salaries and compensation to corporate officers and assistants. It is well established law that a director is not entitled to any pay for his services to the corporation as a director.³ But this rule of law does not prevent the corporation from voting pay to a director, provided the agreement is made before the services are rendered. If the resolution is passed after the director has rendered the services, it cannot be enforced. There can be no back pay.⁴ In New York, it has been doubted whether the directors may in any case vote salaries to one or more of themselves, whether the latter participate in the vote or not.⁵ A resolution

new corporation and a transfer to it of all the assets of the old one may also be a fraud on the creditors of the old corporation. *San F., &c. R. R. Co. v. Bee*, 48 Cal. 398 (1874). A secession of the majority, carrying corporate funds to a new corporation, is a fraud on the old corporation. *Tomlinson v. Bricklayers, &c.*, 87 Ind. 308 (1882).

¹ See § 653, *supra*.

² *Mason v. Pewabic Min. Co.*, 25 Fed. Rep. 882 (1885), holding also that the court will set the transaction aside, order a public sale of the property, and will confirm the first and illegal sale only in case the price then paid exceeds the price offered at the public auction.

³ *Holder v. Lafayette, &c., Ry. Co.*, 71 Ill. 106 (1875). See also *Wood's Railway Law*, § 155.

⁴ *Bennett v. St. Louis, &c., Co.*, 19 Mo. App. 349; s. c., 1 West. Rep. 736 (1885); *Ogden v. Murray*, 39 N. Y. 202 (1868); *Blatchford v. Ross*, 5 Abb. Pr. N. S. 434 (1869). *Cf. Northeastern Ry. Co. v. Jackson*, 19 W. R. 198 (1870), holding that such back pay can be voted only by the stockholders, and that long delay in paying it will nullify the authority, and will require a re-submission of the question to the stockholders. *First Natl. Bk. v. Drake*, 29 Kansas, 311 (1883).

See also *Loan Association v. Stonemetz*, 29 Penn. St. 534; *Citizens' Natl. Bk. v. Elliot*, 50 Iowa, 104 (1880); *Chandler v. Bank*, 13 N. J. L. 255; *Railroad Co. v. Miles*, 52 Ill. 174; *Merrick v. Peru Co.*, 61 Ill. 472; *Railroad Co. v. Sage*, 65 Ill. 328; *Cheney v. Lafayette R. R. Co.*, 68 Ill. 570; 87 Ill. 446; *Linen Co. v. Hough*, 91 Ill. 63; *Henry v. Railroad Co.*, 27 Vt. 435; *Hall v. Railroad Co.*, 28 Vt. 401; *Hodges v. Railroad Co.*, 29 Vt. 220; *Fraylor v. Sonora Co.*, 17 Cal. 594; *Ins. Co. v. Crane*, 6 Met. 64; *Railroad Co. v. Ketchum*, 27 Conn. 170; *Levisse v. Railroad Co.*, 27 La. Ann. 641; *Rogers v. Hastings Co.*, 22 Minn. 25; *Santa Clara Mining, &c., of Baltimore v. Meredith*, 49 Md. 389 (1878); *Bailey v. Buffalo*, 14 Hun, 483; *Jackson v. Railroad Co.*, 2 Thomp. & C. 653; *Gridley v. L. B. & M. R. R. Co.*, 71 Ill. 200; *Kirkpatrick v. Penrose Ferry Co.*, 49 Penn. St. 118; *Butt v. Wood*, 37 N. Y. 316; *Holland v. Bank*, 52 Me. 564; *Manx Ferry Gravel R. Co. v. Branegan*, 40 Ind. 361.

⁵ See *Kelsey v. Sargent*, 40 Hun, 150 (1886), reviewing the cases. The court, however, said: "Without stopping to determine the question as to whether or not the board of directors have the power, by resolution, to vote salaries to one or more of their own body, we are clearly of the opin-

to pay a director for his services is not enforceable, even when made before the services are rendered, if the vote of the director who is interested is necessary to carry that resolution.¹ Where the board of directors vote large pay to themselves, evidently in bad faith, and with a view to depriving the corporation of more than a reasonable proportion of its net earnings, a dissenting stockholder may file a bill in equity to have the amount recovered back.² Or the corporation may defeat the officers' action at law to recover it.³ It has been held also, where the majority of the stock of a corporation was held by one family who voted away the corporate profits for salaries, that the minority might call upon a court of equity to remedy the fraud.⁴

§ 658. *Contracts between corporations having one or more directors in common.*—It has been difficult to determine whether a stockholder in one corporation could cause to be set aside a contract or agreement between two corporations having one or more directors in common. The late and important case of *The*

ion that such salaries so voted are not binding upon the company when the director in whose favor the salary is voted is present participating in the proceeding. In the case under consideration the five directors were present. The motion was carried unanimously. The inference to be drawn from the proceeding is that they all participated. We are consequently of the opinion that, under the circumstances of this case, the salaries voted ought not to be upheld." See also *Dunston v. Imperial Gas Co.*, 3 B. & Ad. 125. But see *MacNaughton v. Osgood*, 24 N. Y. Weekly Dig. 190 (1886).

¹ *Butts v. Wood*, 37 N. Y. 317 (1867); *Ward v. Davidson*, 4 West. Rep. 367 (Mo., 1886), where increased pay was voted to the president of the corporation. *Gardner v. Butler*, 30 N. J. Eq. 702 (1879), where, however, the court says: "The contract will not be regarded, but the services having been rendered, and the company having received the benefit of them, it would be manifestly inequitable to deny to the trustee a fair equivalent for them. If the contract price is reasonable, it will be allowed."

² *Blatchford v. Ross*, 54 Barb. 42 (1869). In the case of *Hodges v. Paquett*, 3 Oreg. 77 (1869), the court refused to interfere, though fraud was charged in that the directors credited large bills to themselves, and paid themselves large sums for services, had destroyed the

business, and had wasted the funds and property. This case, however, has met with universal disapproval, and must be considered as contrary to the law.

³ *Davies v. Memphis City R. R. Co.*, 22 Am. & Eng. R. R. Cas. 1 (Tenn., 1885). In the late case of *Hubbard v. New York, &c., Co.*, 14 Fed. Rep. 675 (1882), wherein a person contracted in advance to become a director and superintendent at a remuneration of one third of the profits of the business, the court refused to uphold the agreement, and said the contract is to be "construed in the same manner as if he was actually a director at the time of its inception, and as if it was made with him while he was a director. A director of a corporation is not absolutely prohibited by law from entering into a contract with the corporation through his co-directors. Whether such a contract is binding upon the corporation must depend upon its terms and the circumstances under which it was made. Owing to the peculiar relation which the directors owe to the corporation, being strictly trustees, and their position being in every sense fiduciary, their contracts with the corporation should be scanned, if not with suspicion, at least with the most scrupulous care."

⁴ *Sellers v. Phoenix Iron Co.*, 13 Fed. Rep. 20 (1881). See also *Pratt v. Jewett*, 9 Gray, 34.

Metropolitan Railway Company against The Manhattan Railway Company¹ clearly establishes the rule that where two corporations

¹ 15 Am. & Eng. R. R. Cas. 1 (1884). The history of this well-known litigation is as follows: The New York Elevated Railroad Co. and the Metropolitan Elevated Railroad Co. leased all their property to the Manhattan Railroad Co., under a lease whereby the latter was to pay to all the stockholders of the former two companies ten per cent. per annum on their stock. It amounted to a guaranteed dividend. Subsequently a minority of the directors of the Metropolitan Co. were also directors in the Manhattan Co. These two corporations then contracted, through their respective boards of directors, to reduce the guaranteed dividend from ten to six per cent. The Metropolitan Company then brought suit to set aside this reduction, and succeeded. Under the same state of facts the Federal court, in *Flagg v. Manhattan Ry. Co.*, 20 Blatchf. 142 (1881), had decided that the stockholder could not have the transaction set aside. But Mr. Justice Van Brunt refused to follow the Federal decision, and in a masterly and exhaustive opinion clearly established the rule given in the text. The court said: "I can see no difference in principle between the case of a director contracting with his corporation and that of directors of one corporation contracting with themselves as directors of another corporation. The evils to be avoided are the same, the temptations to a breach of trust are the same, the want of independent action exists, and the divided allegiance is just as apparent. . . . It may be urged that the position of a director in a corporation does not give him the same degree of personal interest in its success as would be the fact were he simply entering into the contract to be personally benefited thereby; that he is one of many, his interests are divided with that of the stockholders, and his influence may be counteracted by his co-directors. But the fact that he has an adverse interest to the one or the other of the corporations is apparent, and that he is attempting to serve two masters is also equally plain. It must necessarily happen, according to the rules which have been laid down by the courts of equity in reference to the action of agents, that he will, in nine cases out of ten, serve the interest of the one principal and betray those of the other; and, in order to remove persons so situated from all

temptation, in order that there may be no uncertainty in the law in reference to such contracts courts of equity have held that where there is such a conflict of interests between an individual and a corporation, or between corporations having common directors, that the contract shall be voidable as matter of equity, without any evidence whatever of misconduct upon the part of the agent or director. If the rule is to be so far relaxed that common directors may participate in the contracts between corporations, or if common directors may allow contracts to be made between the two corporations that they represent, it would present the same field of speculation and the same uncertainty of result for courts to attempt to investigate the motives of the common directors to determine the influence which they had upon their associates, to determine the fairness and reasonableness of the contract, to investigate all the influences which were at work which led to the entering into the contract, which has been so severely condemned by the cases passing upon the rights of *cestui que trust* in reference to contracts made by common trustees. Contracts of this kind would be left involved in a sea of doubt, and a prediction as to the result of an investigation as to their fairness and honesty would be the merest speculation. It was to relieve the courts from such investigations, and to let parties understand precisely the ground upon which they stood, that the stringent rules in regard to agents and principals were adopted, and the same reasons require that, in order that there may be reasonable certainty in reference to the results to be arrived at in investigating the contracts between two corporations who have common directors, and therefore conflicting interests and conflicting duties, the same rule must be necessarily adopted, namely, that at the option of the *cestui que trust*, or of the corporation, such contract may be voided." For other cases connected with this litigation, see *N. Y. El. R. R. Co. v. Manhattan Ry. Co.*, 14 Abb. N. C. 152, note; *Manhattan Ry. Co. v. N. Y. El. Co.*, 29 Hun, 309, rev'g *N. Y. Daily Reg. Dec. 2, 1882*; *People ex rel. Content v. Metropolitan Ry. Co.*, 26 Hun, 82; *Harkness v. Manhattan Ry. Co.*, *N. Y. Daily Reg. Oct. 8, 1886*. A strong case in support of the same principle is *Pear-*

enter into a contract, such contract may be set aside as fraudulent if, at the time of contracting, the two corporations had one or more directors in common.¹

§ 659. *Foreclosure of mortgage on corporate property, and collusion with directors, whereby no defense is made to the foreclosure.*—A frequent fraud on stockholders, and one which it is difficult to detect and prove, is where the directors collusively neglect to defend against a suit brought to foreclose a mortgage on the corporate property, in consequence of which a default is taken and the corporation speedily deprived of all its assets.² It

son v. Concord R. R. Co., 13 Am. & Eng. R. R. Cas. 102 (N. H., 1883), where the court, in setting aside a contract made by corporations having common directors, said: "Stockholders and creditors are entitled not only to the vote of a director in the board, but to his influence and argument in discussion." Distinguishing *Rolling Stock Co. v. R. R. Co.*, 34 O. St. 465; *Ashhurst's Appeal*, 60 Penn. St. 291; *Watt's Appeal*, 78 Penn. St. 370. See also *Wardens, &c. v. Rector, &c.*, 45 Barb. 356 (1865), where the court said: "When the same person acts in a double capacity as agent or trustee, he must see to it that the transaction is fair and unexceptionable as regards the rights of either of the parties which he so represents. If any motive of personal convenience or interest has been subserved, it will constitute a badge of fraud." In *Bill v. Boston Union Telegraph Co.*, 16 Fed. Rep. 14 (1883), where, however, the fraud was more clear, since the directors common to both corporations constituted a majority of the directors of one of them, the court said: "Undoubtedly the same person may be the agent of two distinct principals, and bind them both by his acts for each; but this is where he is expressly or impliedly authorized to act for each in the transaction with the other." See also *San Diego v. San Diego, &c.*, R. R. Co., 44 Cal. 106 (1872); *Wallace v. Long Island R. R. Co.*, 12 Hun, 460 (1877). *Of. Booth v. Robinson*, 55 Md. 419 (1880), distinguished in *Manhattan, &c., Co. v. Metropolitan, &c., Co.*, *supra*. Also *Mayer, &c. v. Inman*, 57 Ga. 370 (1876), where the town officers merely executed bonds to a railroad company of which they were directors. The bonds were held to be valid.

¹ In *Godin v. Cincinnati & W. Canal*

Co., 18 O. St. 150 (1868), the court well said: "A director whose personal interests are adverse to those of the corporation has no right to be or act as a director. As soon as he finds that he has personal interests which are in conflict with those of the company, he ought to resign. No matter if a majority of the stockholders, as well as himself, have personal interests in conflict with those of the company. . . . He is trustee for the company, and whenever he acts against its interests—no matter how much he thereby benefits *foreign* interests of the individual stockholders, or how many of the individual stockholders act with him—he is guilty of a breach of trust, and a court of equity will set his acts aside, at the instance of stockholders or creditors who are damaged thereby."

² Thompson on Liability of Officers and Agents of Corporations, p. 383, vividly describes such transactions as follows: "Notwithstanding the ready devices with which the courts have met such attempts, this species of roguery has grown into a science with a distinct nomenclature. The interior organization or conspiracy, composed of the holders of a majority of the shares, bent on destroying the rights of the minority, is called a 'ring,' and the business of the conspiracy is called 'wrecking the corporation.' This process of 'wrecking,' which has been seen in many cases of railway corporations, is sometimes carried on in this way. Either the property is allowed to run down, or, under some pretext of improvements, amelioration, or extension of the business, it is 'bonded,' that is to say, negotiable debentures are issued, secured by a mortgage of the corporate property. The scheme is so managed that the majority

is a fraud difficult to detect, since ordinarily there is no defense to foreclosure suits, and the defenses which should have been set up by the corporation are difficult of proof themselves. At an early day the leading case of *Koehler against Black River Fire Insurance Company*,¹ established the principle that a stockholder in

of these debentures find their way into the hands of the 'ring.' The condition of the mortgage is, that whenever default is made in the payment of any of the interest coupons, the mortgage may be foreclosed. This event speedily happens. One of the bondholders now files a bill in equity to foreclose the mortgage, or it is done by the trustee in the mortgage, himself the agent of the 'ring.' The corporation and the directors are made defendants. Now, the directors all being in the 'ring,' the allegations of the bill are admitted in the answer which the corporation makes to the bill, and also those made by the directors. A decree is entered 'by consent' for the sale of the property. This 'consent decree' provides that payment of the purchase money bid at the sale, may be made in the mortgage debentures. The property is sold at auction, is bid in by a member of the 'ring' for the other members, they furnishing him with the bonds, in which he makes payment. Another 'consent decree' is made confirming the sale. The purchaser organizes a new corporation composed of himself and other members of the 'ring,' which takes possession of the property. Now, what has been the result of this proceeding? Simply this: to make further use of the slang in which those who engage in such transactions express themselves, all the stockholders of the old corporation not in the 'ring' are 'squeezed out.' The property has been sold under a mortgage. The common stock has become valueless. Those of the stockholders who, with the directors, were in the conspiracy, have got it all, and those who were out of it, have lost all. Thus, the chancellor not only has not circumvented the rogue, but the rogue has made the chancellor his tool in the accomplishment of his nefarious purpose. I speak deliberately in saying that this is no imaginary picture. More than one astute railroad lawyer, when he reads this, will, from his own experience, be compelled to admit that I have held the mirror up to nature."

¹ 2 Black, 715 (1862), where the directors took a mortgage to themselves to

secure debts due to them from the corporation, and then foreclosed. The foreclosure was defeated. So also in *Bayliss v. Lafayette, &c. R. R. Co.*, 8 Biss. 198 (1878), where the directors were silent partners with the construction company mortgagees. The court, on the application of a stockholder, directed that the mortgagees be allowed only the amount honestly due them; and see *Mussina v. Goldthwaite*, 34 Texas, 125 (1870), where, there having been a fraudulent foreclosure suit instituted, the court said: "We think that an intervenor, claiming an interest in the subject-matter in dispute, may interpose his claim as a defendant to the suit, having been made such by leave of the court, the better to protect his interests; and if there be fraud and collusion between the original parties, whereby his interests are compromised or prejudiced, he may set it up affirmatively and prove it, and thereby defeat any fraudulent design intended to be carried out by the suit." In the case, however, of *Samuel v. Halladay*, 1 Woolw. 600 (1869), where a sale under foreclosure had been made after an advertisement of five weeks, the court refused to set it aside for fraud in the foreclosure proceedings, although on the sale only one-fifth of the value of the property was realized; and in *Forbes v. Memphis, &c. Ry. Co.*, 2 Wood, 323 (1872), the court said: "It is questionable whether, in any case where a suit is properly instituted against a corporation, a stockholder of that corporation can, even on a suggestion of fraud on the part of its officers, come in by way of intervention as party to that suit, and seek to defend or control the proceedings. An original bill would rather seem to be the proper mode of proceeding. . . . It is in the discretion of the court whether or not to permit a stockholder to become a party defendant in any case where he is not made such by the bill." In *Drury v. Cross*, 7 Wall. 299 (1868), a foreclosure and sale was set aside where it was obtained by an agreement to release the directors from liability as indorsers. See also *Bronson v. La Crosse R. R. Co.*, 2

such a case may be allowed to come in as a defendant, and set up the defenses which the corporation ought to have set up. Another remedy of the stockholder is to redeem the property before the foreclosure sale, and then give the corporation a reasonable time to redeem the property from him, or be forever barred from its rights therein.¹ In Pennsylvania,² and New Jersey,³ however, it has been doubted whether the stockholder would be allowed to intervene in a fraudulent foreclosure suit, the court saying that his remedy is to have the judgment set aside for fraud. In New York, by statute, the courts have power to allow the stockholder to come in as a party defendant.⁴ A stockholder cannot cause a foreclosure sale to be set aside, on the ground of corrupt motives of the directors who allowed the default to be taken, unless he can show collusion between them and the purchaser at the foreclosure sale.⁵ Where the corporation brings a suit to redeem its

Wall. 283, 302 (1863), where the court said: "Undoubtedly, in the case supposed, it would be a reproach to the law, and especially in a court of equity, if the stockholders were remediless. But in such a case, the court in its discretion will permit a stockholder to become a party defendant, for the purpose of protecting his own interests against unfounded or illegal claims against the company; and he will also be permitted to appear on behalf of other stockholders who may desire to join him in the defense. But this defense is independent of the company and of its directors, and the stockholder becomes a real and substantial party to the extent of his own interests and of those who may join him, and against whom any proceeding, order, or decree of the court in the cause is binding, and may be enforced. It is true, the remedy is an extreme one, and should be admitted by the court with hesitation and caution; but it grows out of the necessity of the case, and for the sake of justice, and may be the only remedy to prevent a flagrant wrong." In *Blackman v. Central R. R., &c. Co.*, 58 Ga. 189 (1877), the court said: "That the action is groundless and collusive, and that, from motives of fraud or favor on the part of the officers, the corporation fails or refuses to defend, will make no difference. The stockholders may protect all their rights by instituting a proper action of their own." In the very recent case of the *Union Trust Company v. Rochester & Pittsburgh R.*

Co. (U. S. C. C. Pittsburgh, Dec. 6th, 1886), 1 *Railway & Corporation Law Journal*, 15, it was held that the defense of a collusive foreclosure judgment herein, in a State court, cannot be set up to defeat an action thereon in a Federal court. See *Pittsburgh, &c. R. R. Co. v. Rothschild*, 4 *Central Rep.* (Penn. 1886).

¹ *Wright v. Oroville M. Co.*, 40 Cal. 20 (1870), where the court, on the stockholder's application, fixed the time within which the corporation must redeem, if at all.

² *Gavenstine's Appeal*, 49 Penn. St. 310 (1865), where the court said: "When a company authorizes a debt, and it is created by and with the assent of all the stockholders, as well as the board of directors, and judgment has been confessed by the same authority, I see not much room for equitable interference by a stockholder so consenting. But suppose he may be able to make out a case for interference by showing fraud or mistake in the judgment, why can he not have ample remedy by applying to the court in which the judgment is entered, to open or set aside the judgment?" To same effect, *County of Tazewell v. Farmers, &c., Trust Co.*, 12 *Fed. Rep.* 752 (1882).

³ *Brown v. Vandyke*, 8 N. J. Eq. 795 (1853).

⁴ *Code of Civil Procedure*, § 452. See *Ithaca Gas Light Co. v. Treman*, 93 N. Y. 660 (1883).

⁵ *Harpending v. Munson*, 91 N. Y. 650 (1883).

property from a foreclosure sale, a stockholder has no right to come in as a party complainant.¹

§ 660. *Directors' purchases of property needed by the corporation.—Buying up the debts of the corporation, and loans to the corporation.*—It is an abuse of trust for a corporate director to purchase property which he knows the corporation will need, and then to sell the same to the corporation at an advanced price. This generally occurs, where the director purchases in his own name land which the corporation must purchase for its enterprise, or over which it will need a right of way.² Where, however, the director offers the land to the corporation at the price which he paid for it, and the corporation refuses it, he cannot long subsequently be compelled to accept that price.³ It is a fraud on the corporation and on corporate creditors for the directors to buy up at a discount the outstanding debts of the corporation, and compel it to pay them the full face value thereof. In such a case, the directors may be compelled to turn over to the corporation the evidences of indebtedness upon being paid the money which they gave for the same.⁴ There is nothing, however, illegal or fraudulent in a loan by the directors to the corporation, and the taking of a mortgage on the corporate property as security therefor.⁵

¹ Kennebec, &c. R. R. Co. v. Portland, &c. R. R. Co., 54 Me. 173 (1866). If a collusive judgment for an ordinary cause of action has been entered against the corporation it may be set aside. Whittlesey v. Delaney, 73 N. Y. 571 (1878).

² Blake v. Buffalo Creek R. R. Co., 56 N. Y. 485 (1874), where the court said: "Occupying this relation of trust toward the corporation and its stockholders, these directors were bound, in all matters pertaining to the construction of the road and the acquisition of the roadway, to act as the representatives, and for the benefit of the company. Well settled rules forbade their acquiring, for themselves, the property, which it was their duty to acquire for the company, and which was necessary for its purposes. Such a dealing would be equally objectionable, as purchasing from the company land which it was their duty to sell on its behalf. In respect to this class of dealings, directors of corporations stand upon the same footing as ordinary trustees. . . . It is a rule of equity of universal application, that no person can

be permitted to purchase an interest in property, when he has a duty to perform in relation to such property which is inconsistent with the character of a purchaser." See Buffalo, &c. R. R. Co. v. Lampson, 47 Barb. 533 (1867); Blair, &c. Co. v. Walker, 50 Iowa, 376 (1879); Taylor v. Solomon, 4 Mylne & C. 134 (1838), where the corporate agent took in his own name a lease which the company desired, and had instructed him to obtain for itself. See also Mitchell v. Reed, 61 N. Y. 123 (1874).

³ Sandy River R. R. Co. v. Stubbs, 77 Me. 595 (1885).

⁴ Duncomb v. N. Y. &c. R. R. Co., 84 N. Y. 190, 202 (1881); *Ex parte* Larking, 46 L. J. (Ch.) 235 (1877). See also Davis v. Rock, &c. Co., 55 Cal. 359 (1880); *Cf.* Bradley v. Marion, &c. Co., 3 Hughes, 26 (1879).

⁵ Duncomb v. N. Y. &c. R. R. Co., 88 N. Y. 1 (1882); 84 Id. 190; Hotel Co. v. Wade, 97 U. S. 13 (1877); Hope v. Salt Co., 25 W. Va. 789 (1885); *Ex parte* Hill, L. J. (Ch.) 154 (1863), holding also that an additional rate of interest is not

§ 661. *Embezzlement and misuse of corporate funds by directors.*—It is clearly established, and would hardly seem to need argument that where the corporate directors have embezzled or used the corporate funds for their own purposes, and still retain control of the corporation, that a stockholder may institute a suit in chancery to compel them to refund the funds so used. This is perhaps the simplest application of the doctrine that a stockholder's suit will be sustained where the corporation is powerless to enforce its rights. In the early and important case of *Robinson v. Smith*,¹ Chancellor Walworth sustained a stockholder's action to hold the corporate directors liable for corporate funds lost by speculation in the stocks of other corporations.² So also a stockholder's action lies where the directors owe large sums to the corporation, and refuse to pay or charge themselves with the same, and are about to sell the corporate property at a sacrifice.³

§ 662. *Frauds by a majority of the stockholders upon the minority.*—In addition to frauds arising by the illegal purchase of the corporate property by a majority of the stockholders, there may arise other fraudulent acts by the majority. The law requires of them the utmost good faith in their contract and management of the corporation, as regards the minority, and in this respect the majority stand in much the same attitude towards

enforceable, so far as the excess of interest is concerned. See also *Twin Lick Oil Co. v. Marbury*, 91 U. S. 587; *Hallam v. Indianola Hotel Co.*, 56 Iowa, 178; *Claflin v. South Carolina R. R. Co.*, 4 Am. & Eng. R. R. Cas. 231; *Harpending v. Munson*, 91 N. Y. 650 (1883). Cf. *Wilbur v. Lynde*, 49 Cal. 290 (1874). A sale of corporate bonds to a syndicate of which three of the directors are members is valid, the price being adequate. *Du Pont v. Northern Pac. R. R. Co.*, 18 Fed. Rep. 467 (1883), per Wallace, J. See § 653, *supra*.

¹ 3 Paige Ch. 222 (1832).

² The court said: "Until very recently, but few incorporated companies, in which individuals had any direct pecuniary interest, existed in England, except corporations for charitable purposes. . . . The directors are the trustees or managing partners, and the stockholders are the *cestuis que trust*. . . . No injury the stockholders may sustain by a fraudulent breach of trust, can, upon the

general principles of equity, be suffered to pass without a remedy. . . . As this court never permits a wrong to go unredressed merely for the sake of form, if it appeared that the directors of the corporation refused to prosecute by collusion with those who had made themselves answerable by their negligence or fraud, or if the corporation was still under the control of those who must be made the defendants in the suit, the stockholders, who are the real parties in interest, would be permitted to file a bill in their own names, making the corporation a party defendant." See also *Combination Trust Co. v. Weed*, 2 Fed. Rep. 24 (1880); *Hardon v. Newton*, 14 Blatch. 376 (1878); *Smith v. Rathbun*, 29 Hun, 150 (1880); *Land Credit Co. v. Lord Fermoy*, 17 W. R. 562.

³ *Sears v. Hotchkiss*, 25 Conn. 171 (1856). See also *Hardon v. Newton*, 14 Blatch. 376 (1878), involving somewhat similar facts.

the minority, that the directors sustain towards all the stockholders. Thus, where the majority are interested in another corporation, and the two corporations have contracts between them, it is fraudulent for that majority to manage the affairs of the first corporation for the benefit of the second. A court of equity will intervene and protect the minority upon an application by the latter.¹ So also where the officers of another corporation, which has leased the property of the first corporation, control a majority of the stock of the latter, and conspire to compel the minority to sell their stock by refusing to pay the rent due on the lease, a court of equity, on the application of the minority, will compel a payment of the rent.² A late and most satisfactory case involving frauds by a majority of the stockholders upon the minority, is *Ervin against The Oregon Railway and Navigation Company*,³ which clearly enounces and sustains the doctrine that

¹ *Menier v. Hooper's Tel. Works, L. R. 9 Ch. 350* (1874). See also *Peabody v. Flint*, 6 Allen; *Gorham v. Gilson*, 28 Cal. 479 (1865); *Rice's Appeal*, 79 Penn. St. 168 (1875), the court said: "Where a person has the actual control of a corporation, whether such control arises from the ownership of a majority of the shares, or from his position or influence, enters into a contract with such corporation, he is to be held to the most rigid good faith. The *onus* is upon him to show the fairness of the transaction if it is called in question. It is a principle too well settled to be now successfully controverted, that the promoters, directors, or agents of a company, shall not make a profit out of it in buying lands for it, or in dealing with it."

² *Barr v. N. Y., &c., R. R. Co.*, 96 N. Y. 444 (1884). Judge Thompson, in his work on the Liability of Officers and Agents of Corporations gives a true description of such transaction when he says, p. 384: "Another species of fraud, by no means infrequent, presents a history like the following: The managers of a wealthy and powerful railroad corporation, desiring to get possession of a rival, or a connecting line, succeed in purchasing a majority of the shares of the stock of the latter company. They then install themselves, or their agents, as its directors. These directors, in violation of their duty to the shareholders of the company, manage its affairs entirely in the interest of the former company, and to the pre-

judice of those of its shareholders who are not interested in the former company. Unless a court of equity could interfere to prevent such an abuse, the rights of the shareholders in the smaller company would be placed in a perilous condition. 'For it would enable the managers of one corporation to get control of another by the purchase of a majority of its stock for the purpose, and then to manage its affairs in such subservience to the interest of their own corporation as to render the stock of the minority worthless, and avail themselves of its value without compensation.' If such frauds may be practiced with impunity, it requires no sagacity to see how 'a system of railroad connections may become a system of frauds. If it may be practiced with impunity between railroad corporations, it may be practiced between manufacturing corporations, and a managing majority may, at their pleasure, sacrifice the interests of the minority for the benefit of another corporation owned by them.'"

³ 27 Fed. Rep. 625 (U. S. C. C. New York, 1886), per Wallace, J.; s. c. 20 Fed. Rep. 577. In this case the majority placed a valuation upon the property of the corporation, dissolved the corporation, and sold the property to themselves at the price fixed. The learned judge set aside the sale, and adjudged that the minority had an equitable lien on the property to the extent of the actual value of the property sold. In the opinion the court said: "Plainly, the defendants have

“when a number of stockholders combine to constitute themselves a majority in order to control the corporation as they see fit, they became for all practical purposes the corporation itself, and assume the trust relation occupied by the corporation towards its stockholders.”

§ 663. *Stockholders' actions against third persons for frauds against the corporation.*—Ordinarily where third persons have defrauded a corporation, and have defrauded it by collusion with the corporate officers, the stockholder's action is

assumed to exercise a power belonging to the majority in order to secure personal profit for themselves, without regard to the interests of the minority. They repudiate the suggestion of fraud, and plant themselves upon their right as a majority to control the corporate interests according to their discretion. They err if they suppose that a court of equity will tolerate a discretion which does not consult the interests of the minority. It cannot be denied that minority stockholders are bound hand and foot to the majority in all matters of legitimate administration of the corporate affairs; and the courts are powerless to redress many forms of oppression practiced upon the minority under the guise of legal sanction, which falls short of actual fraud. This is a consequence of the implied contract of association, by which it is agreed, in advance, that a majority shall bind the whole body as to all transactions within the scope of the corporate powers. But it is also of the essence of the contract that the corporate powers shall only be exercised to accomplish the objects for which they were called into existence, and that the majority shall not control those powers to pervert or destroy the original purposes of the corporators.” So also where the majority of the stockholders vote to make a lease of the whole corporate property to themselves, a dissenting stockholder may have the lease set aside. *Meeker v. Winthrop Iron Co.*, 17 Fed. Rep. 48 (1883), the court saying: “The ownership of a majority of the capital stock of a corporation invests the holders thereof with many and valuable incidental rights. They may legally control the company's business, prescribe its general policy, make themselves its agents, and take reasonable compensation for their services. But in thus as-

suming the control they also take upon themselves the correlative duty of diligence and good faith. They cannot lawfully manipulate the company's business in their own interests to the injury of other corporators. Any contract made by them in behalf of their principal with themselves or with another for their personal gain would be voidable at the option of the company. . . . If they can make such a lease, they can, as selfishness or caprice shall dictate, modify its terms, expend the company's entire income in improvements to facilitate their individual interests, or do anything else their selfishness or cupidity may suggest. The law does not thus vest majority stockholders with any such dangerous power, invite such speculations or open the door to such abuses.” And in *Rice's Appeal*, 79 Penn. St. 168, 204 (1875), the court said: “While the right of a stockholder to contract with his corporation and become its creditor, is conceded as a general proposition, the right of a person controlling the corporation to contract with it, rests upon entirely different principles, if it exists at all. Where a person has the actual control of a corporation, whether such control arises from the ownership of a majority of the shares, or from his position or influence, and enters into a contract with such corporation, he is to be held to the most rigid good faith. The *onus* is upon him to show the fairness of the transaction, if it is called in question.” Where, however, corporate property has been sold, and the proceeds retained by one stockholder, another stockholder cannot sue him for money had and received. The action must be in equity and for the benefit of the corporation. *Hodsdon v. Copeland*, 16 Me. 314 (1839).

against both the officers and the third persons, all being joined as parties defendant. When such is the case the cause of action comes under some one of the preceding sections of this chapter.¹ Another class of cases arise when third persons commit frauds against the corporation without the collusion of the corporate officers, but the latter neglect or refuse to institute a suit to rectify the wrong. The right of the stockholder then is not so clear. It is ordinarily within the discretion of the corporate officers to enforce, compromise, or abandon claims which the corporation may have against third persons. Generally this exercise of discretion cannot be questioned or remedied by the stockholders, except by electing, at a subsequent election, directors more in accord with the stockholders' views. It is possible, however, that cases may occur, where the judgment of the directors is so palpably and injuriously wrong, the courts will sustain a stockholder's action herein. This subject, however, is treated elsewhere.²

¹ Thus where a railroad has been leased to another railroad company, under a certain agreement of the latter guaranteeing a fixed sum to the former, and the lessee railroad company refuses to fulfill its contract and has control of the lessor railroad, a stockholder of the latter may bring suit against the former to remedy the wrong. *March v. Eastern R. R. Co.*, 40 N. H. 548 (1860). And the case of *Lewis v. St. Albans, &c, Works*, 50 Vt.

477 (1878), very properly says, "that whenever the trustee has been guilty of a breach of trust, and has transferred the trust property by sale or otherwise, to any third party, the *cestui que trust* has a full right to follow such property into the hands of such third party, unless he stands in the situation of a *bona fide* purchaser for value, without notice."

² See Chapter XL, § 678.

CHAPTER XL.

STOCKHOLDERS' ACTION TO REMEDY ULTRA VIRES ACTS, INTRA VIRES ACTS, AND NEGLIGENCE OF CORPORATE DIRECTORS AND OTHERS.

A.—ULTRA VIRES ACTS.

- § 664. Meaning of the term *ultra vires*.
- 665. The three contracts arising from a charter.
- 666. The third contract, that between the stockholders and the corporation prevents the commission of *ultra vires* acts.
- 667. Neither the directors nor a majority of the stockholders have power to sell all the corporate property as against the dissent of a single stockholder.
- 668. Consolidations, absorptions, mergers, amalgamations, leases, and sales of railroads without authority of charter, statute, or amendment of charter.
- 669. Consolidation, lease, or sale under express provision in the charter itself.
- 670. Consolidation, sale, or lease under authority of a general statute existing at the time of incorporation.
- 671. Consolidation, lease, or sale under an amendment to the charter or under a general statute passed subsequent to the charter.
- 672. Stockholder's right to prevent the corporation from undertaking a new business.
- 673. Traffic arrangements and contracts.

- § 674. Giving away or misapplying corporate funds.
- 675. Miscellaneous *ultra vires* acts.

B.—A STOCKHOLDER CANNOT REMEDY THROUGH THE COURTS, ANY ACTS INTRA VIRES OF THE DIRECTORS, OR A MAJORITY OF THE STOCKHOLDERS, SINCE THEY ARE MATTERS OF INTERNAL MANAGEMENT.

- § 676. *Intra vires* acts as distinguished from *ultra vires* acts.
- 677. The discretion of the directors or the majority of the stockholders as to acts *ultra vires* cannot be questioned by the courts, unless fraud is involved.
- 678. The discretion of the directors in refusing to institute or to defend an action involving corporate interests is not generally interfered with.

C.—STOCKHOLDERS' ACTIONS TO HOLD THE DIRECTORS LIABLE FOR NEGLIGENCE IN THE DISCHARGE OF THEIR DUTIES.

- § 679. Remedy of the stockholder herein.
- 680. Instances of negligence of directors in the performance of their duties.
- 681. Directors must use ordinary care and diligence in the management of the corporation and the transaction of its business.

A.—ULTRA VIRES ACTS.

§ 664. *Meaning of the term ultra vires.*—The term *ultra vires*, as used in this treatise, means any act of a corporation which the corporation is not authorized to do, either by its express or implied powers. This definition includes acts beyond the powers of the corporation, whether these acts are prohibited

by statute, or are contrary to public policy and good morals, or are merely not among the powers given to the corporation by its charter. This term has been objected to as having no fixed and clear meaning, and to some extent the objection is reasonable.¹ There is no other term, however, that has acquired the significance, general use, and peculiar meaning that are attached to the words *ultra vires*, and consequently the term probably has acquired a permanent place in the vocabulary of corporation law.

§ 665. *The three contracts arising from a charter.*—It has already been explained² that the charter of a corporation is the basis of three distinct contracts; first, between the corporation and the State; second, between the stockholders and the State; and third, between the stockholders and the corporation. The first named contract, that between the corporation and the State, does not come within the scope of this work. The great and leading case on that contract in this country is the Dartmouth

¹ In the case *Taylor v. Chichester, &c., Ry. Co., L. R., 2 Ex. 356, 378 (1867)*, the court said: "I think it very unfortunate that the same phrase of '*ultra vires*' has been used to express both an excess of authority, as against the shareholders and the doing of an act illegal, as being *malum prohibitum*, for the two things are substantially different." The term *ultra vires* has at times been used in two senses by one and the same court. Thus it is said in *Bissell v. Railroad Companies*, 22 N. Y. 258, 293 (1860): "The phrase *ultra vires* is applied, in the English cases, both to acts which simply exceed the powers conferred by the deed of settlement upon the officers, as the agents of the shareholders, and acts which transcend the powers conferred by law upon the entire corporation. This indiscriminate use of the phrase is calculated to mislead, unless the distinction referred to is observed." In the case *National Pemberton Bk. v. Porter*, 125 Mass. 333, the court says: "There is nothing of mystery or of sanctity in the use of the words of a dead language, *ultra vires*; and although it is a concise and convenient form by which to indicate the unauthorized action of artificial persons with limited powers, still it is as applicable to individual as to corporate action. An illegal act of an

individual is as really *ultra vires* as the unauthorized act of a corporation."

In the case *Whitney Arms Co. v. Barlow*, 63 N. Y. 62 (1875), the court said: "Where acts of corporations are spoken of as *ultra vires*, it is not intended that they are unlawful or even such as the corporation cannot perform, but merely those which are not within the powers conferred upon the corporation by the act of its creation, and are in violation of the trust reposed in the managing board by the shareholders, that the affairs shall be managed and the funds applied solely for carrying out the objects for which the corporation was created." See also *Earl of Shrewsbury v. North Staffordshire R. Co.*, 35 L. J. (Ch.) 166; *Nassau Bk. v. Jones*, 95 N. Y. 115 (1884). In *Green's Brice's Ultra Vires*, 2d ed. p. 35, the learned author says: "Sometimes the term *ultra vires* is used even in a fourth sense, as denoting what is outside the powers, not of a particular corporation, but of every corporation. By-laws in restraint of trade are *ultra vires* in this sense. Facts will thus be *ultra vires* which are contrary to the common law or to the provisions express or implied of some statute, *e. g.*, the issuing prior to the companies act of 1867 of shares to bearer."

² See Chapter XXVIII.

College case.¹ In England, no such contract exists, since Parliament is not restricted by any written constitution, and the power of Parliament to alter, amend, or repeal charters is absolute.² As regards the second contract, in this country, the better, later, and prevailing opinion is that an amendment of a charter by the legislature, whether under a reserved power or not, cannot be forced upon the corporation or stockholders, and cannot even be accepted by the directors or by a majority of the stockholders in opposition to the dissent of a single stockholder. This is upon the principle that the amendment merely waives the right of the State to object to acts which without the amendment would be unauthorized by the charter; that the waiver of the State of its right to insist on its contract or charter with the corporation and stockholders does not waive, change, or affect the contract between the corporation and the stockholders; and that, consequently, the amendment does not take away the right of a stockholder to object to the change, but that he may object thereto, the same as he may object to any *ultra vires* act, except that his objection must be based on the violation of his contract with the corporation, and not upon the danger of the State's forfeiting the corporate charter. Hence it is, that from a stockholder's point of view an amendment to the charter may be objected to by him, very largely upon the same grounds and to the same extent that he may object to *ultra vires* acts. In both cases, his objection rests upon the basis that the change violates his contract with the corporation.³

§ 666. *The third contract, that between the stockholders and the corporation prevents the commission of ultra vires acts.*—That a charter constitutes a contract between the corporation and its stockholders is a principle of law that has become firmly imbedded in the jurisprudence of modern times. Upon this principle of law rests the stability, permanence and honesty of management of many corporations, particularly those of railroads, and from it arises much of the confidence, safety, and protection of the stockholder himself. It was first promulgated in America, in

¹ 4 Wheat. 518 (1819).

² "Parliament created this company, and I think the power must rest with Parliament to vary the constitution of the company, to control it, to annihilate, or

to deal with it as in its wisdom it shall think fit." *Great Western Ry. Co. v. Rushout*, 5 De G. & Sm. 290 (1852).

³ See Chapter XXVIII.

1820, in *Livingston v. Lynch*,¹ and was applied to corporations in *The Hartford & New Haven Railroad Company* against *Croswell*,² and in England, in 1824, in *Natusch v. Irving*.³ These cases have been followed by a long list of supporting decisions. They were the first to establish clearly the doctrine that any act or proposed act of the corporation, or of the directors, or of a majority of the stockholders which is not within the express or implied powers of the charter of incorporation or of association, in other words, any *ultra vires* act is a breach of the contract between the corporation and each one of its stockholders, and that consequently any one or more of the stockholders may object thereto and compel the corporation to observe the terms of that contract as set forth in the charter.⁴

§ 667. *Neither the directors nor a majority of the stockholders have power to sell all the corporate property as against the dissent of a single stockholder.*—The case of *Abbot v. American Hard Rubber Company*⁵ clearly established the rule in this country that a dissenting stockholder may prevent the sale by the directors, or by a majority of the stockholders, of corporate property which is essential to the continuance of the business of the corporation, unless such sale is made with a view to the dissolution of the corporation, or the payment of the corporate debts.⁶

¹ 4 Johns. Ch. 373.

² 5 Hill, 383 (1843).

³ 2 Cooper's Ch. 358, by Lord Eldon; also reported in *Gow on Partnership*, 398. Thus Lord Chancellor Campbell said, in *Simpson v. Westminster Palace Hotel Co.*, 8 H. of L. Cases, 712 (1860): "I bow to the authority of *Natusch v. Irving*. . . . The funds of a joint-stock company established for one undertaking cannot be applied to another. If an attempt to do so is made, this act is *ultra vires*, and although sanctioned by all the directors and by a large majority of the shareholders, any single shareholder has a right to resist it, and a court of equity will interfere on his behalf by injunction." In *Pickering v. Stephenson*, L. R., 14 Eq. 322 (1872), the court said: "It is difficult to conceive any system of jurisprudence in which *Natusch v. Irving* would have been differently decided." This case also held that when the majority enter into litigation against the minority, costs are not to be paid by majority out of the corporate funds.

⁴ The jurisdiction of a court of chancery to protect a stockholder against *ultra vires* acts is now established beyond question, and this jurisdiction exists irrespective of statutes. In New York, however, at an early day in the case, *Attorney-General v. Utica Ins. Co.*, 2 Johns. Ch. 389, it was held that a court of chancery had no such visitatorial power over corporations as to restrain them from exceeding their corporate powers. The Revised Statutes of New York, in 1828, gave to the courts this jurisdiction. See *Brinkerhoof v. Bostwick*, 88 N. Y. 52, 59 (1882).

⁵ 33 Barb. 578 (1861). See also *Id.* 4 Blatch. 489.

⁶ See also *Smith v. New York, &c. Co.*, 18 Abb. Pr. 419 and 435 (1865); *Robbins v. Clay*, 33 Me. 132; *Hat B. Co. v. Eickmeyer, &c.*, 56 How. Pr. 78; *Barclay v. Quicksilver M. Co.*, 9 Abb. Pr. N. S. 284; *Copeland v. C. Gas Co.*, 61 Barb. 60; *Conro v. Port Henry I. Co.*, 12 Barb. 127; *Adriance v. Rooms*, 52 Barb. 399; *Brady v. Mayor, &c.*, 16 How. Pr.

And even where a dissolution is the purpose in view, yet if the corporation is a prosperous one, it is extremely doubtful whether such a sale can be made. The old common law doctrine that a majority of the stockholders may at any time effect a voluntary dissolution of the corporation is still sustained. But if the purpose of such dissolution is not the *bona fide* discontinuance of the business, but is the continuance of that business by another new corporation, then the better and later rule is that a dissenting stockholder may prevent the sale, even though it is made with a view to dissolution of the corporation. This is the law as laid down by the well-considered case of *Kean v. Johnson*.¹ Such a dissolution is practically a fraud on the law and on dissenting stockholders. It seeks to do indirectly what cannot legally be done directly.² If, however, the corporation is an unprofitable and failing enterprise, then a sale of all the corporate property with a view to dissolution may be made by a majority of the stockholders.³ But although the sale may be made even to another corporation yet the stock of the latter cor-

432; *Middlesex R. R. Co. v. Boston, &c., R. R. Co.*, 115 Mass. 347. *Of. Dana v. Bk. of U. S.*, 5 Watts & S. (Pa.) 247; *Union Bank, &c. v. Ellicott*, 6 Gill & J. (Md.) 363. See also *Sheldon, &c. Co. v. Eickemeyer, &c. Co.*, 90 N. Y. 607 (1882); *Balliet v. Brown*, 103 Penn. St. 546 (1883), where the court says: "The directors of a corporation have no right to sell or dispose of its movable property where this prevents the continuance of their business." To same effect *Gray v. N. Y., &c. Steamship Co.*, 5 T. & C. (N. Y.) 224 (1875). But see *Hutchinson v. Green* (Mo. 1886), 1 Ry. & Corp. Law Journal, 22.

¹ 9 N. J. Eq. 401 (1853), the court saying it is not true that "a majority of stockholders in any corporation, however prosperous its business affairs may be, can, at their own mere caprice, sell out the whole source of their emoluments, invest their capital in other enterprises, and that however the minority may desire the prosecution of the business in which they had engaged, they have no injury to complain of at law or in equity so long as they obtain their portion of the proceeds of the sale. . . . If such were the law, corporations would soon be few, for seldom would capitalists, whatever their comparative wealth, invest in enterprises so readily rendered profitless at

the caprice or in obedience to the interest of any man or set of men rich enough to control the majority of stock. . . . Sometimes no time is fixed by the charter at which the proposed use of the capital shall cease, and then the contract between the parties is that so long as the affairs of the company are prosperous it shall go on, unless all consent to the contrary." Even where the majority have a statutory power to dissolve the corporation at their pleasure, yet they cannot use that power to defraud the minority out of the fair value of the corporate property. *Ervin v. Oregon Ry. & Nav. Co.*, 27 Fed. Rep. 635, (1886), per Wallace, J., the court saying: "A dissolution under such circumstances is an abuse of the powers delegated to the majority. It is no less a wrong because accomplished by the agency of legal forms."

² *Boston, &c. R. R. Co. v. N. Y. & N. E. R. R. Co.*, 13 R. I. 260 (1881).

³ *Lauman v. Lebanon Valley R. R. Co.*, 30 Penn. St. 42 (1858), the court saying: "Can one member of a corporation hold all his fellow-members, with their investments, to an unprofitable and impracticable enterprise and prevent them from embarking in another that is more hopeful? No; their power of dissolution will relieve them from such an objection."

poration received in payment for the property cannot be forced upon dissenting stockholders. They are entitled to money.¹ These principles of law are particularly important when a consolidation of corporations is attempted by a dissolution of one of them. Frequently such a sale of the corporate property is attempted without a dissolution, the vendee of the property agreeing to pay the stockholders of the vendor corporation. Such a sale, however, is voidable at the instance of a single stockholder.² Corporations are formed for the transaction of business and not for the purpose of having their business transacted by other corporations.

§ 668. *Consolidations, absorptions, mergers, amalgamations, leases, and sales of railroads without authority of charter, statute, or amendment of charter.*³—By far the greater number of

¹ *Lauman v. Lebanon, &c. Co.*, *supra*; *Taylor v. Earle*, 8 Hun, 1 (1876); *Frothingham v. Barney*, 6 Hun, 366. *Cf.* *Treadwell v. Salisbury, &c., Co.*, 78 Mass. 393 (1856); *Hodges v. New England, &c. Co.*, 1 R. I. 312 (1850); 3 Id. 392 (1853). See also § 646.

² See § 668.

³ There has been considerable discussion as to the meaning of these various terms. The only practical object of such discussions seems to be in ascertaining whether the old corporation is dissolved or is continued, and in ascertaining similar questions. These questions, however, turn upon the wording of the statute or charter whereby the change is made. In general it may be said that by a consolidation, merger, or amalgamation, either two corporations are dissolved and a new one formed therefrom, or one is dissolved and its property and franchises are taken up by another. In Indiana it was held that the effect of a consolidation "was a dissolution of the three corporations and at the same instant the creation of a new corporation, with property, liabilities, and stockholders, derived from those passing out of existence." *McMahan v. Morrison*, 16 Ind. 172. See also *Clearwater v. Meredith*, 1 Wall. 25, 40 (1863). *Cf.* *Meyer v. Johnston*, 64 Ala. 603; *Central R. R. Co. v. Georgia*, 92 U. S. 665; *Racine, &c. R. R. Co. v. Farmers, &c. Trust Co.*, 49 Ill. 331. In *Boardman v. Lake Shore, &c. Ry. Co.*, 84 N. Y. 157, 181 (1881), the court said: "It is held that where two railroads are consolidated, as far as one of the creditors of one of the

original companies is concerned, the consolidated company is the successor of the old company; but in respect to the properties of the other companies it is a new and independent company, and such creditor has no claim against it upon their original contract, but only by virtue of its assumption of the obligations of the old companies." Citing *Prouty v. L. S., &c. R. R. Co.*, 52 N. Y. 363; *Chase v. Vanderbilt*, 62 Id. 307; *In re Sage*, 70 Id. 220. In *Green's Brice's Ultra Vires*, 2d ed., p. 631, it is said: "The term 'amalgamation' is seldom applied to corporations in this country. That which takes its place as much as any is 'consolidation.' But, though it is difficult accurately to define amalgamation as commonly used in English law, it certainly has a wider meaning than consolidation has with us. Consolidation would, *e. g.*, be inapplicable to a union of two or more companies in such a way that one of the original corporations only was continued in existence, while the others were merged or absorbed in it. An absorption of one corporation by another would, according to some of the decisions, be an amalgamation in England; but it would not be a consolidation here. . . . In the American view, therefore, it would seem that the dissolution of all the old corporations and the creation of one new one are as a rule involved in consolidation. And this idea must not be overlooked in determining the rights of creditors. For if all the corporations, cease the consolidated company is liable to the creditors

cases involving *ultra vires* acts which affect the rights of a stockholder are cases growing out of the attempted consolidation, absorption, lease or sale of the property of one railroad corporation by or with another railroad corporation. The rapid tendency of the railway system towards the creation and unification of trunk lines, and the annihilation of smaller companies, has led to many of these cases. The interests in such movements frequently involve vast amounts of property. In Europe this stage of railway development has been passed through, and it is there generally found that in each country a few great systems control all the railways of the country. In America the past twenty years have brought about the creation of semi-transcontinental lines, and the consolidation, absorption, and disappearance of large numbers of local or branch lines. But the American movement towards systems of railways which will traverse the entire continent is already clearly outlined and at hand. The changes which are impending will lead to the disappearance of existing short lines and even systems of railways. Large interests will require and in some way will obtain a removal of the legal right of stockholders to object to the changes toward which the times are rapidly approaching. The principles of law protecting the rights of stockholders in these attempted consolidations or leases are to be of vital importance, both to the railroads and to the stockholders themselves.

These consolidations, absorptions, leases, or sales of railroads have occurred or have been attempted under four different claims of legal right or authority. These are, first, under the claim that there is an implied power of the corporation to make the change; second, that the charter expressly confers this right; third, that

of each, in the absence of special agreement, only so far as it is assignee of its property, while if one is continued in existence the debts of that one which continue would seem to burden the whole property however acquired." In the case *Dongan's Case*, 28 L. T. N. S. 60 (1873), the court said: "Two companies may be united, either by fusion into a third or by one absorbing the other. The former process seems to correspond most nearly with the popular sense of the word amalgamation, and I believe nobody really knows what amalgamation means. Whatever be the process no shareholder in the company which it destroys, or of which

it suspends the life, can become a shareholder in the other company without his personal assent." In the case *Fee v. Gas Company*, 35 La. Ann. 413 (1883), the court said: "The articles of consolidation, and the legislative act by authority of which they were executed, evidently present a case of complete and perfect amalgamation, the effect of which was, under American authorities, to terminate the existence of the original corporations, to create a new corporation, to transmute the members of the former into members of the latter, and to operate a transfer of the property, rights, and liabilities of each old company to the new one."

a general statute, existing at the time of incorporation, expressly authorized the act; fourth, that an amendment to the charter, or a general statute passed subsequently to the incorporation, expressly authorized the consolidation, absorption, sale, or lease.

It is a principle of law, clearly established and now unquestioned, that neither the directors of a corporation nor a majority of the stockholders can, as against one or more dissenting stockholders, authorize a sale of the corporate property to another corporation, unless express authority for the sale is conferred by the charter, or a constitutional amendment thereto, or a statute constitutionally applicable to that charter. There is no *implied* power to make such a sale.¹ Moreover, a sale or lease of one railroad to another, without the express authority of the legislature, is an *ultra vires* act as regards the State also;² and for such an act, without doubt, the State may intervene, forfeit the franchises of the first corporation for non-user, and assume the eminent domain franchises that have been transferred.³

So also a lease of one railroad to another, without express authority from the legislature, is beyond the power of the directors or a majority of the stockholders, as against a dissenting stockholder. It is a violation of the implied contract between the corporation and each stockholder that the business prescribed in the charter will be *pursued* until the dissolution of the corpo-

¹ Clinch v. Financial Corporation (1868), L. R. 5 Eq. 450; Kean v. Johnson, 9 N. J. Eq. 401 (1853). In this case a statute authorized the consolidating sale, if it could be made legally. The court held that it could not be. See also Charlton v. Newcastle, &c., Ry. Co., 5 Jur. N. S. 1096 (1859); Tuttle v. Michigan, &c., R. R. Co., 35 Mich. 247 (1877); International, &c., R. R. Co. v. Bremond, 53 Texas, 96 (1880), holding, however, that the directors are not personally liable therefor. Blatchford v. Ross, 54 Barb. 42 (1869); Dongan's Case, 28 L. T. N. S. 60 (1873); Boston, &c., R. R. Co. v. New Eng. R. R. Co., 13 R. L. 260 (1881), where the sale was declared to be illegal, though the stockholder's road was in the hands of mortgagees for default in the payment of interest, the old stockholders being offered stock in a new corporation, or a fixed sum for their shares of stock. Laches, however, in complaining, was held to be fatal. Atlantic, &c., R. R. Co. Case, 3 Hughes, 320; Id., 4 Hughes

(N. S.), 151 (1878), holding that where the consolidating sale is unauthorized, a stockholder of the old corporation is not affected by a foreclosure sale of all the property of the new corporation. This case is valuable as containing approved forms for pleadings and decrees in the procedure, appointment of receiver, and sale and distribution of assets upon the foreclosure of a railroad mortgage. In the case of Bryson v. Warwick, &c., Co., 1 Sm. & G. 447 (1853), it was held that a stockholder in a corporation might sue in equity to recover back for the corporation forfeit money paid by it to another corporation on an *ultra vires* contract to purchase the latter.

² Abbott v. Johnstown, &c., R. R. Co., 80 N. Y. 27 (1880); Troy, &c., R. R. Co. v. Boston, &c., Ry. Co., 86 N. Y. 107 (1881); Thomas v. Railroad Co., 101 U. S. 71 (1879); Penn. R. R. Co. v. St. Louis, &c., N. R., 118 U. S. 290 (1886).

³ See § 496; People v. Albany, &c., R. R. Co., 77 N. Y. 232 (1879).

ration. Generally the lease of a railroad is made under an agreement, whereby the stockholders of the old corporation are guaranteed a certain income. The effect, however, is not a continuation of the business of the old corporation, but an abandonment of it. It is an act *ultra vires* of the corporation, and in violation of the contract between the corporation and its stockholders. A single stockholder may obtain an injunction against the lease, or if it is already made, may go into a court of equity to have it set aside.¹

§ 669. *Consolidation, lease, or sale under express power in the charter itself.*—If the charter of a corporation expressly authorizes a lease or sale of the corporate property, such a lease or sale may be made by a majority of the stockholders in meeting assembled, and the minority are bound thereby. It is immaterial what the terms of the sale or lease may be, or whether they be advantageous or disadvantageous to the stockholders. The dissenting minority have no remedy unless actual fraud can be shown. Thus a lease, made under such a charter provision, has been upheld, although the rental from the lease will pay dividends only on the preferred stock, leaving nothing whatsoever for the common stockholders.²

§ 670. *Consolidation, sale, or lease under authority of a general statute existing at the time of incorporation.*—There seems to be little doubt that if, at the time of an incorporation of a company, there is a general statute on the statute book authorizing the consolidation, sale, or lease of one railroad to another,

¹ *Winch v. Birkenhead, &c., Ry. Co.*, 5 De G. & Sm. 562 (1852), where the lease was for 99 years. *Cass v. Manchester, &c., Co.*, 9 Fed. Rep. 640 (1881), where the lease was for 5 years. *Stevens v. Davison*, 18 Gratt. (Va.) 819 (1868); *McDonnell v. Grand Canal Co.*, 3 Ir. Chan. N. S. 578 (1853); *South Georgia, &c., R. R. Co. v. Ayres*, 56 Ga. 230 (1876); *Tippecanoe County v. Lafayette, &c., R. R. Co.*, 50 Ind. 85 (1875); *Black v. Delaware, &c., Canal Co.*, 24 N. J. Eq. 455 (1873); rev'g 22 N. J. Eq. 130. In this last important, leading, and clearly-reasoned case, the court says: "Nor is the difficulty avoided by the proposition that a corporate body, by and with the assent of a majority of the corporators, may abandon their business. Even if this was true, upon such dissolu-

tion the franchises could not be transferred, but would revert to the sovereignty from which they were derived, and the shareholders would become partners or joint-owners in the assets, and for their share in such assets they could not be compelled to accept an annual rent for nine hundred and ninety-nine years."

² *Middletown v. Boston, &c., R. R. Co.*, 2 New Eng. Rep. 553 (Conn., 1886). See also *Gates v. Id.*, 1 Id. 464 (Conn., 1886), where the charter allowed leases on a three-fourths vote of the stockholders. It may be remarked that when such acts can be done under the sanction of the law, there is occasion for protection of the minority's rights by legislative enactment.

then such consolidation, sale, or lease may be made even against the dissent of a minority of the stockholders. The law has been held to be such in England,¹ Indiana,² and New York.³ Generally the statute which authorizes the sale, lease, or consolidation of railways provides for the payment of money to a dissenting stockholder who prefers to close out his interest in the matter rather than take part in the new enterprise.⁴ A lease or sale, however, under the authority of such a statute, is a corporate act so fundamental in its nature that it is to be exercised, not by the directors, but only by the stockholders in meeting assembled. So also a subsequent change in the terms of the contract of sale or lease can be made, not by the directors, but by the stockholders themselves.⁵

§ 671. *Consolidation, lease, or sale under an amendment to the charter or under a general statute passed subsequent to the charter.*—It has already been shown in a preceding chapter⁶ that an amendment to a charter, whereby a consolidation of the corporation with another corporation is authorized, can be accepted and acted upon by the corporation only by the unanimous consent of the stockholders.⁷ A single dissenting stockholder

¹ *Simpson v. Denison*, 10 Hare, 51 (1852), where the court says that when a statute exists authorizing such corporate changes, "every person who becomes a shareholder in such a company must be considered as holding, and contracting to hold these shares, subject to the provisions of this statute."

² *Bish v. Johnson*, 21 Ind. 299 (1863); *Sparrow v. Evansville, &c.*, R. R. Co., 7 Ind. 369 (1856).

³ *Metropolitan, &c., Ry. Co. v. Manhattan, &c., Ry. Co.*, 15 Am. & Eng. R. R. Cas. 1, 26 (1884). In New York a general statute was passed in 1839 (Laws 1839, ch. 218), which, after much doubt, has been held to authorize a lease of one railroad to another. See *Troy & Boston R. R. Co. v. Boston, Hoosac Tunnel, &c., R. R. Co.*, 86 N. Y. 107 (1881); *Abbott v. Johnstown, &c., R. R. Co.*, 80 N. Y. 27 (1880); *Woodruff v. Erie Ry. Co.*, 93 N. Y. 609 (1883). A statutory authority to sell a business to a company has, however, been held not to authorize a sale to an individual. *Bird v. Birds, &c., Sewage Co.*, L. R. 9 Ch. 358 (1874). As to the law in Illinois, see *Ottawa, &c., R. R. Co. v. Black*, 79 Ill. 262 (1875).

⁴ Such is the statutory law in Pennsylvania. Brightley's *Purdon's Digest*, 1223. In New York, chapter 917, Laws 1869, authorizing consolidations, does not contain such a provision. In England, a provision to that effect is found. See *Ex parte Fox*, L. R. 6 Ch. 176 (1871).

⁵ *Metropolitan El. Ry. Co. v. Manhattan El. Ry. Co.*, 15 Am. & Eng. R. R. Cas. 1 (N. Y., 1884), where Van Brunt, J., says that the lease could be made only by the stockholders, and that "if the board of directors could not make a new lease upon definite terms and conditions, then, clearly, they could not radically modify the old lease." See also *Harkness v. Manhattan Ry. Co.*, N. Y. Daily Reg., Oct. 8, 1886. Cf. *People v. Metropolitan Ry. Co.*, 26 Hun, 84 (1881).

⁶ Chapter XXVIII.

⁷ See § 500, note 1. See also *Clearwater v. Meredith*, 1 Wall. 25, 39 (1863), where the court says: "In conferring the authority, the legislature never intended to compel a dissenting stockholder to transfer his interest because a majority of the stockholders consented to the consolidation. Even if the legislature had manifested an obvious purpose to do so,

may enjoin a consolidation made under such circumstances. The better opinion also is that this rule prevails even though the legislature has reserved the right to alter or amend the charter. The reserved right is to make amendments for the benefit of the public, and not for the benefit of the majority as opposed to the minority of the stockholders.¹ The legislature, corporation, and majority, however, are not entirely subject to the will of dissenting stockholders. Under the power of eminent domain the legislature may, in a statute authorizing consolidations, leases, or sales of railroads, provide therein that a dissenting stockholder's stock shall be appraised and condemned, thereby removing all obstacles to the proposed act. Such a condemnation proceeding is legal and constitutional.² But a statute giving authority to condemn stock, for the purpose of effecting a consolidation of corporations, is no authority for the condemnation where only a lease is being effected; nor have the courts any power to award damages to the dissenting stockholder, and then take from him his stock.³

In England there is no restriction on the power of Parliament to amend a charter, and the courts will not enjoin an application to Parliament for an amendment,⁴ but will enjoin any use of corporate funds to aid and further that application.⁵

the act would have been illegal, for it would have impaired the obligation of a contract." *Mayor, &c., of Knoxville v. Knoxville, &c., R. R. Co.*, 22 Fed. Rep. 758. Where also the stockholders have unanimously consented to a lease under such a statute, the terms of the lease cannot be materially changed without the unanimous consent of the stockholders. *March v. Eastern R. R. Co.*, 43 N. H. 515 (1862); *s. c.*, 40 N. H. 548.

¹ See § 501. Also *Buffalo, &c., R. R. Co. v. Dudley*, 14 N. Y. 336, 354 (1856).

² *Black v. Delaware, &c., Canal Co.*, 24 N. J. Eq. 455 (1873); *rev'g* 22 N. J. Eq. 130, under the Act of 17th March, 1870.

³ *Mills v. Central R. R. Co.*, 41 N. J. Eq. 1 (1886).

⁴ *Heathcote v. North Staffordshire Ry. Co.*, 2 McN. & G. 100. See also *McDonnell v. Grand Canal Co.*, 3 Ir. Ch. Rep. N. S. 578 (1853).

⁵ *Simpson v. Denison*, 10 Hare, 51 (1852); *Maunsell v. Midland, &c., Ry. Co.*, 6 Hem. & M. 130 (1863); *Great Western Ry. Co. v. Rushout*, 5 De G. & Sm. 290

(1852). In England the doctrine has been enounced that the principle that the majority cannot bind the minority as to an act not within the common contract does not apply "to corporate companies for a public undertaking, involving public interests and public duties, under the sanction of Parliament. In such cases the court of chancery has permitted the use of the corporate seal and the moneys of the company to obtain the sanction of Parliament to purposes materially altering the interests of the shareholders according to the contract *inter se*." *Stevens v. South Devon Railway Company* (13 Beav. 48). . . . There can be no doubt of the soundness of the principle that the directors and the majority of a company may be restrained from employing money subscribed for one purpose in prosecution of another, however advantageous. That is a general principle founded on the law of contract; but, like other general principles, it is subjected in its application to many qualifications." *Ffooks v. Southwestern Ry. Co.*, 1 Sm. & G. 142 (1853).

§ 672. *Stockholder's right to prevent the corporation from undertaking a new business.*—It is *ultra vires* of a corporation to undertake to carry on a business which is not fairly within the scope of the business described in its charter. When such an attempt is made on the part of the directors or a majority of the stockholders, a dissenting stockholder may insist upon the corporate business being confined to the limits of the corporate charter, and he may enjoin or set aside any acts which do not conform to those limits. Thus, a corporation formed to manufacture iron cannot go into the flour and mill business,¹ and a railroad company cannot improve a river, although it has power to build wharves.² A stockholder in a plank road company may enjoin his company from running a stage line and carrying the mails,³ and a stockholder in a railroad company may enjoin it from subscribing for stock in another company.⁴ A railroad cannot go into the water transportation business without releasing all dissenting stockholders from their subscription,⁵ nor can a life insurance company extend its business to fire and marine insurance.⁶ So also where a railroad company is about to extend its line beyond the limits fixed by the charter, a dissenting stockholder may enjoin it from so doing.⁷ But a reasonable use of the profits to provide additional facilities for the business cannot be objected to or enjoined by a minority of the stockholders.⁸

§ 673. *Traffic arrangements and contracts.*—At an early day it was decided that an agreement and contract of two companies to carry on business in common, and divide the profits in

¹ *Cherokee Iron Co. v. Jones*, 52 Ga. 276 (1874).

² *Munt v. Shrewsbury, &c., Ry. Co.*, 13 Beav. 1 (1850).

³ *Wiswall v. Greenville, &c., R. R. Co.*, 3 Jones' Eq. (N. C.) 183 (1857).

⁴ *Mannuell v. Midland, &c., Ry. Co.*, 1 Hem. & M. 130 (1863); or buying stocks, *Central R. R. Co. v. Collins*, 40 Ga. 332 (1869); *Salomons v. Laing*, 12 Beav. 339 (1849). See Chapters IV, XIX, &c., and there are many other similar acts which are *ultra vires* acts, and which the stockholders may enjoin. They have been treated and explained in the various chapters of this work, under appropriate headings, *q. v.*

⁵ *Hartford & New Haven R. R. Co.*

v. Croswell, 5 Hill, 383 (1843), per Nelson, C. J.

⁶ *Ashton v. Burbank*, 2 Dill. 435.

⁷ *Bagshaw v. Eastern Union Ry. Co.*, 7 Hare, 114 (1849). Even though the extension be authorized by an amendment. See *Stevens v. Rutland, &c., R. R. Co.*, 29 Vt. 545 (1851).

⁸ *Pratt v. Pratt*, 33 Conn. 446 (1866), the court saying: "On a question of this sort much must necessarily be left to the discretion of the managing directors, and so long as they keep within the objects contemplated by the articles of association, and the expenditure is not unreasonable in reference to the amount of their capital, a court of equity ought very seldom to interfere with them."

a certain proportion was *ultra vires* and illegal, and could be enjoined by a single stockholder of either corporation.¹ But this rule has been doubted and weakened in England by subsequent decisions.² It has been held that a stockholder may enjoin action under a contract whereby his corporation allows another to lay rails and do business over the former company's right of way.³ In this country the question does not seem to have yet been fairly raised by a dissenting stockholder.⁴ In Minnesota it has been held that traffic arrangements between two railroads are not *ultra vires* and illegal as a matter of law, but that the question is a mixed one of law and fact. A stockholder who objects must bring suit within a reasonable time or he will be denied relief.⁵

§ 674. *Giving away or misapplying corporate funds.*—It is *ultra vires* and illegal for the board of directors to donate the funds of the corporation to charitable or public purposes, or to aid corporations of a similar character, however praiseworthy the purpose of the donation may be.⁶ Nor can the directors legally use the funds of the corporation to induce promoters to abandon a proposed rival company.⁷ A stockholder may enjoin the direc-

¹ *Charlton v. Newcastle, &c., Ry. Co.*, 5 Jur. N. S. 1096 (1859).

² See *Hare v. London, &c., Ry. Co.*, 2 J. & H. 80; 1 Id. 252 (1860); *Hodgson v. Earl Powis*, 1 De G., M. & G. 6; *Lancaster, &c., Ry. Co. v. North Western Ry. Co.*, 2 K. & J. 293; *Shrewsbury, &c., Ry. Co. v. North Western Ry. Co.*, 4 De G., M. & G. 115. In 1846, the court in *Colman v. Eastern Counties Railway Company* (10 Beav. 1), well said, "Companies of this kind, possessing most extensive powers, have so recently been introduced into this country, that neither the legislature nor courts of justice have been yet able to understand all the different lights in which their transactions ought properly to be viewed. We must, however, adhere to ancient general and settled principles, so far as they can be applied to great combinations and companies of this kind. . . . It has been very properly admitted that railway companies have no right to enter into new trades or businesses not pointed out by their acts; but it has been contended that they have a right to pledge without limit the funds of the company for the encouragement of other transactions, however various and extensive, provided the

object of that liability is to increase the traffic upon the railway, and thereby to increase the profit to the shareholders. There is, however, no authority for any thing of that kind." And the court held that a stockholder might enjoin his corporation from guaranteeing certain profits to another company.

³ *Beman v. Rufford*, 6 Eng. L. & Eq. 106 (1851), the court saying, "I will not allow any speculation that it would be more advantageous to do something which the Act of Parliament does not authorize to be done."

⁴ *Morrill v. Boston, &c., R. R. Co.*, 55 N. H. 531, seems to have been under a statute. In New Jersey, pooling arrangements seem to be considered lawful. *Sussex R. R. Co. v. Morris, &c., R. R. Co.*, 19 N. J. Eq. 13. Cf. *Hartford, &c., R. R. Co. v. N. Y., &c., R. R. Co.*, 3 Robt. (N. Y.) 411.

⁵ *Stewart v. Erie, &c., Trans. Co.*, 17 Minn. 372 (1871).

⁶ *Polar Star Lodge v. Polar Star Lodge*, 13 La. Ann. 53 (1861); *Ward v. Davidson*, 1 Southwest. Rep. 846 (Mo. 1886).

⁷ *Russell v. Wakefield Waterworks Co. L. R.*, 20 Eq. 474 (1875), holding also

tors from making free of tolls, a bridge from which the corporation derives its income.¹ The directors may be held liable for allowing the president to use the corporate funds for lobbying purposes.² An unreasonable use of the corporate profits of a leased railroad to build up and improve the lessor railroad, without reference to the rights of the former, has been held to be good cause of complaint on the part of a stockholder in the leased railroad company.³ And, in general, any misapplication or waste of the property of a corporation may be remedied by a member thereof.⁴

§ 675. *Miscellaneous ultra vires acts.*—It has been a difficult question whether a change of the location or route of a railroad company by the directors or the majority of the stockholders is an *ultra vires* act which a stockholder may complain of. The prevailing opinion seems to be that it is *ultra vires* if the change is a material one.⁵ And there are many other acts, which the stockholders may remedy, as being *ultra vires*. Any act of the corporation that will render the charter liable to forfeiture, or leavy fines and penalties, may be enjoined by a stockholder.⁶ But a stockholder cannot prevent the corporation from applying to one purpose moneys raised for another purpose.⁷ Nor can he compel a cessation of work by the corporation, merely because it has not completed its line within the time prescribed by the charter.⁸ Nor can he prevent a reasonable application of the profits of the company to an extension of the business.⁹ But he may enjoin the organization of the company, when it is about to be made by a fraud on the law and on the State.¹⁰ And it has been held that

that the promoters may be made parties defendant, and be compelled to refund the money.

¹ East Rome, &c., Co. v. Nagle, 58 Ga. 474 (1877).

² Shea v. Mabry, 1 Lea (Tenn.), 319 (1878), and the case York, &c., Ry. Co. v. Hudson, 16 Beav. 485 (1853), held a director liable to the corporation for money used for "secret service" purposes. The court said, "If the defendant has applied the property of the company in a manner which will not bear the light, and for purposes which cannot, with propriety, be stated even to the shareholders of the company, and which purposes have not been distinctly sanctioned by them, the defendant must bear the consequences."

³ March v. Eastern R. R. Co., 43 N. H. 515 (1862); s. c. 40 N. H. 548.

⁴ Armstrong v. Church Society, 13 Grant Ch. (U. C.) 552 (1867).

⁵ See §§ 187, 429, 500; Board, &c., of Tippecanoe Co. v. Lafayette, &c., R. R. Co., 50 Ind. 85 (1875).

⁶ Bliss v. Anderson, 31 Ala. 612 (1858).

⁷ Yetts v. Norfolk Ry. Co., 3 De G. & Sm. 293 (1849).

⁸ Ffooks v. South. &c., Ry. Co., 1 Sm. & G. (1853).

⁹ See § 541.

¹⁰ Cass v. Ottawa, &c., Ins. Co., 22 Grant (U. C.), 512 (1875), the capital stock not having been paid in as certified in the certificate.

he may enjoin the company from proceeding to build a part only of the line of railroad prescribed by the charter.¹ It has been held that a stockholder in a hotel company cannot enjoin the managers from leasing a part of the property for other purposes, there being sufficient accommodation left for the hotel.² But a single stockholder in a railroad corporation may enjoin it from building another line which it has no charter power to build.³ The stockholder may enjoin any act on the part of the State which is in violation of the charter which it granted to the corporation. It was to enjoin a tax by the State under such circumstances that the case of *Dodge v. Woolsey*⁴ arose. An injunction will also be granted at the instance of a stockholder to prevent the corporation from giving a mortgage which would be *ultra vires*.⁵ And it has been held that a stockholder may enjoin his corporation from paying money to a rival company to induce the latter to discontinue business.⁶

B.—A STOCKHOLDER CANNOT REMEDY THROUGH THE COURTS, ANY ACTS INTRA VIRES OF THE DIRECTORS, OR A MAJORITY OF THE STOCKHOLDERS, SINCE THEY ARE MATTERS OF INTERNAL MANAGEMENT.

§ 676. *Intra vires acts as distinguished from ultra vires acts.*—An *ultra vires* act, as already explained, is an act beyond the express and implied powers of the corporation. An *intra vires* act, on the contrary, is one which is within the express or implied powers, either of the board of directors or of the majority of the stockholders in meeting assembled. The *intra vires* acts are frequently spoken of as matters concerning the “internal management” of the corporation. Much confusion has arisen concerning these acts, owing to a failure to recognize clearly the fact that an act is *intra vires* of a corporation, if it can legally be carried out *either* by the directors or by the majority of the stockholders. Thus, a stockholder frequently brings suit to enjoin or set aside an act which the majority have power to do, but which the directors have done without power. It is clear that a dissenting stock-

¹ *Cohen v. Wilkinson*, 1 Mac. & G. 481 (1849).

² *Simpson v. Westminster, &c., H. Co.*, 8 H. L. C. 712 (1860).

³ *Bagshaw v. Eastern Union Ry. Co.*, 7 Hare, 114 (1849).

⁴ 18 How. 331 (1855).

⁵ *McCalmont v. Phil. &c., R. R. Co.*, 3 Am. & Eng. R. R. Cas. 163 (U. S. C. C. 1881).

⁶ *Leslie v. Lorillard*, 40 Hun, 392 (1886).

holder has no right to carry such a matter into the courts, unless the majority are with him, since if the majority approve of the directors' acts, this amounts to a ratification of the same.

In short there are three classes of corporate acts herein. First, the stockholder may bring suit to remedy an act which is *ultra vires* or beyond the powers of both the majority of the stockholders and of the directors. Second, as to acts within the power of the majority, but beyond the power of the directors, a stockholder may sue to enjoin or set them aside, when the directors have performed them and the majority refuse to confirm their action.¹ As to such acts, the stockholder cannot sue, if the majority confirm the directors in their performance. Third, as to acts within the powers of the directors and performed by them or within the powers of the majority, and performed by the majority, the stockholders cannot complain that they are *ultra vires*. The second and third classes of acts are *intra vires* of the corporation. They are matters of internal arrangement or management, and cannot be controlled or objected to by a single stockholder.² The question

¹ *Exeter & C. Ry. Co. v. Buller*, 11 Jur., Part I, 527, 532 (1847), holding also that where such an action has been instituted, it will not be defeated by the fact that subsequently the directors obtain control of a majority of the votes. But there must be clear proof that the majority refuse to confirm. Thus in *Bagshaw v. Eastern Union Ry. Co.*, 7 Hare, 114 (1849), the court says that *Foss v. Harbottle*, 2 Hare, 495, decides "that if the act, though it be the act of the directors only, be one which a general meeting of the company could sanction, a bill by some of the shareholders on behalf of themselves and others, to impeach that act, cannot be sustained, because a general meeting of the company might immediately confirm and give validity to the act of which the bill complains." See also *McDougall v. Gardiner*, L. R., 1 Ch. D. 18 (1875).

² Thus in *Bloxam v. Metropolitan Ry. Co.*, L. R., 3 Ch. 337 (1868), the court says: "The matters of internal arrangement which are beyond the province of the court were properly admitted to be such as are within the scope of the company's powers." And in *Camblos v. Phil. & R. R. Co.*, 4 Brews. 563 (U. S. C. Ct., 1873), the court said: "So long as those who manage the corporation keep

within the limits of their charter, and commit, or propose to commit, no breach of their trust, he has no right to complain." In the case *Becher v. Wells, &c., Co.*, 1 Fed. Rep. 276 (1880), it was said: "A court of equity will not interfere with the internal policy of a corporation unless it is manifest that the proposed act is *ultra vires*." In *Bach v. Pacific, &c., Co.*, 12 Abb. Pr. (N. S.) 373 (1872), the court said: "No case can be found where the general management of corporate property has been subject to the restrictions of judicial power, unless, indeed, in the case of a clear violation of express law; or a wide departure from chartered powers." In this case the stockholder objected to the securities in which the corporate funds were being invested. In *Walker v. Mad River, &c., Ry. Co.*, 8 O. 38 (1887), it was said by the court: "When acts requiring judgment, science, and professional skill are confided to the discretion of the officers of a corporation the exercise of that discretion will not be lightly disturbed." In *Tuscaloosa Mfg. Co. v. Cox*, 68 Ala. 71 (1880), the court said: "To allow a dissatisfied minority to arraign the directors before the courts of the country, whenever in the opinion of such minority a wiser or better policy could have been pursued, would practi-

of what *intra vires* acts are to be performed by the directors, and what ones can be exercised only by the majority of the stockholders in meeting assembled, has been considered elsewhere.¹

§ 677. *The discretion of the directors or the majority of the stockholders as to acts intra vires, cannot be questioned by the courts, unless fraud is involved.*—This proposition of law is clearly, firmly, and very properly established beyond any question. Were the rule otherwise, there would be no safety or possibility of carrying on business through corporations. There would be suits instituted by dissatisfied stockholders on slight provocation and sometimes for the very purpose of embarrassing the transaction of business. A partner in a copartnership may prevent action which he disapproves, but corporations are formed very largely to avoid that very danger and disadvantage. The corporate directors, so long as they act within their powers may use their own discretion as to what ought to be done. Such also is the rule with the majority of the stockholders in meeting assembled. An act *intra vires* and without fraud is an act of internal management, and a minority of the stockholders are powerless to prevent, control, change, or question that act. Thus a stockholder has no remedy for the mere inefficiency of a director, except at the elections of the corporation. Having once been elected, a director is entitled to retain his position even though he be grossly inefficient, provided he is not guilty of fraud or *ultra vires* acts.² But where there are violent internal dissensions in a corporation, and two sets of officers are attempting to

cally put an end to the benefits claimed to result from associated capital. . . . If it be supposed an unwise course is being pursued, or that the interests of the corporation are suffering or likely to suffer through the inefficiency or faithlessness of an official, an appeal should first be made to the directory or governing body, to redress the grievance. Failing there, in ordinary cases the next redress will be found in the power of the ballot, which usually comes into exercise at short intervals," and in *Ramsey v. Erie Ry. Co.*, 7 Abb. Pr. (N. S.) 156 (1869), it is said: "When directors are only unwise or merely extravagant or improvident, or slightly negligent, or

merely misjudge in the performance of their duties, the remedy of stockholders is to elect other persons directors in their places." In *Bailey v. Birkenhead, &c.*, Ry. Co., 12 Beav. 433 (1849), where a stockholder sought to restrain a call as being unnecessary, the court refused to entertain the suit and said that it was not for the court "to take upon itself to determine a question, which might well and ought to be determined by the shareholders themselves at general meetings." See also *Edwards v. Shrewsbury, &c.*, Ry. Co., 2 De G. & Sm. 537 (1848).

¹ See §§ 621-627.

² See *Gorman v. Guardian Sav. Bk.*, 4 Mo. App. 180 (1877).

act, and the corporate property is endangered, a court of equity will interfere to the extent of preserving the corporate property by a temporary receiver.¹ A court of equity cannot, however, restrain the corporation from proceeding with business and using its funds for that purpose, even though a minority of the stockholders can show that sound business discretion and judgment would dictate a different policy.²

§ 678. *The discretion of the directors in refusing to institute or to defend an action involving corporate interests is not generally interfered with.*—It frequently happens, that the corporation has a cause of action against a third party which the directors think best not to press, or that the corporation is sued and the directors think best not to defend, or where an action is pending, the directors decide to compromise the matter. The judgment of the directors may, in the opinion of a stockholder, be erroneous, and yet it cannot be controlled or changed by the stockholders except by refusing to re-elect the directors to office. The stockholder cannot go into court and attempt to change the policy of the directors as regards the management of the suit.³ In general, a corporation represents and binds the shareowners in bringing and defending suits which involve the rights and obligations of the corporation, and binds them as fully as in the making of contracts.⁴

¹ Trade Auxiliary Co. v. Vickens, L. R., 16 Eq. 308 (1873); Featherston v. Cooke, Id. 298, the court saying: "The court will not interfere with the internal affairs of joint-stock companies unless they are in a condition in which there is no properly constituted governing body, or there are such dissensions in the governing body that it is impossible to carry on the business with advantage to the parties interested. In such a case the court will interfere, but only for a limited time, and to as small an extent as possible." See also Lawrence v. Greenwich, &c., Co., 1 Paige, 587 (1829).

² Fountain Ferry, &c., Co. v. Jewell, 8 B. Monr. (Ky.) 140 (1847), the court saying: "The question of expediency, of practicability, of extravagance, or of prudent economy, must be left to be decided by the managers and the corporators."

³ "There may be claims against di-

rectors; there may be claims against officers; there may be claims against debtors; there may be a variety of things which a company may well be entitled to complain of, but which, as a matter of good sense, they do not think it right to make the subject of litigation, and it is the company, as a company, which has to determine whether it will make anything that is wrong to the company, a subject-matter of litigation, or whether it will take steps itself to prevent the wrong from being done. MacDougall v. Gardiner, L. R., 1 Ch. D. 13 (1875).

⁴ Farnum v. Ballard, &c., Shop, 12 Cush. 507 (1853); Oglesby v. Attrill, 105 U. S. 605 (1881); Came v. Brigham, 39 Me. 35 (1854); Lane v. Weymouth School Dist. 10 Metc. 462 (1845); Graham v. Boston, Hartford & Erie R. R. Co., 118 U. S. 161 (1886); affirming s. c. 14 Fed. Rep. 753 (1888).

Thus it is not for the stockholder to institute a suit for a trespass against the corporate property;¹ nor can he take out an appeal or *certiorari* which the corporation does not take out;² nor bring an action against other corporate agents for injury and loss to the corporation.³ The great case of *Dodge v. Woolsey*,⁴ however, was on the very point now under discussion, and it was decided under the facts of that case, where the corporation refused to defend itself against an illegal tax, that a stockholder of the corporation might do that which the corporation should have done.⁵ It is within the power of the directors to compromise a pending law suit by or against the corporation, and a stockholder cannot control the directors' decision.⁶

It has been held, however, that a stockholder may bring suit on behalf of the corporation, to remove a cloud from the corporate title to real estate,⁷ and that a stockholder may sue for the corporation to compel delinquent stockholders to pay in their unpaid subscriptions.⁸ In one case it has been held that, where there is a controversy among the stockholders as to how many directors one of the stockholders, a municipality, is entitled to, a stockholder may file a bill to settle it, since the corporation is not bound to decide or test the matter.⁹

The rule which ordinarily prevents a stockholder from instituting or defending a suit against third persons herein, is clearly

¹ *Dale v. Grant*, 34 L. J. 142 (1870).

² *Silk Mfg. Co. v. Campbell*, 27 N. J. L. 539 (1859).

³ *Forbes v. Whitlock*, 3 Edw. Ch. 446 (1841).

⁴ 18 How. 331 (1855), where the court said: "Now, in our view, the refusal upon the part of the directors, by their own showing, partakes more of disregard of duty, than of an error of judgment. It was a non-performance of a confessed official obligation, amounting to what the law considers a breach of trust, though it may not involve intentional moral delinquency." See also *Memphis, &c., Bo. v. Williamson*, 9 Heisk. (Tenn.) 314 (1872), where suit was brought on the bond which the plaintiff in *Memphis City v. Dean* (8 Wall. 73), gave in obtaining an injunction.

⁵ See also *Park v. Petroleum Co.*, 25 W. Va. 108 (1884); *Id.*, 26 Id. 486 (1885).

⁶ "It cannot be contended that the directors of a corporation do not possess

authority, acting in good faith, and in the exercise of their best judgment, to settle a pending action, or that the settlement is not binding on their stockholders, even though it may subsequently appear that they failed to secure the best terms to which the corporation might have been entitled." *Donohue v. Mariposa, &c., Co.*, 66 Cal. 317 (1885). See also *Shawhan v. Zinn*, 79 Ky. 300 (1881).

⁷ *Baldwin v. Canfield*, 26 Minn. 43, 56 (1879).

⁸ *Wallworth v. Holt*, 4 Mylne & C. 619 (1840), the Lord Chancellor saying: "I think it the duty of this court to adapt its practice and course of proceeding to the existing state of society, and not by too strict an adherence to forms and rules, established under different circumstances, to decline to administer justice, and to enforce rights for which there is no other remedy."

⁹ *City of Wheeling v. Mayor of Baltimore, &c.*, 1 Hughes, 90 (1862).

to be distinguished from all other classes of actions treated of in the fourth part of this work. The actions now being considered are those which exist for or against the corporation in a multitude of cases, and which are of daily occurrence to all great corporations. They are actions not involving frauds or *ultra vires* acts of the directors, but involve, at the most, only a neglect of the directors to begin or defend suits.

There is a class of cases which are midway between these two classes. This third class involves both a neglect of the directors to defend a suit against the corporation, and they involve the further fact that the defense is not made on account of the fraud and collusion of the directors with the complainants in the suit. This generally happens in foreclosures of mortgages on the property of the corporation, a subject which has already been treated.¹

C.—STOCKHOLDERS' ACTIONS TO HOLD THE DIRECTORS LIABLE FOR NEGLIGENCE IN THE DISCHARGE OF THEIR DUTIES.

§ 679. *Remedy of the stockholder herein.*—Where, by reason of the negligence of the directors or other officers, the corporate funds, property, or rights, have been lost, the injury is practically and ultimately an injury to the stockholders. But, in the eye of the law, the injury is to the corporation itself. The loss has depleted its treasury, just as a profit from the business would be for the benefit of that treasury. Moreover, the negligent act was in reference to the affairs of the corporation, and was an injury to the corporation. Accordingly, it is for the corporation to call the directors to an account for their negligence. The action is not an action which the stockholder is to bring. The negligence affects him, not directly but indirectly, by the injury to the corporation. Hence, the law is well settled that a stockholder cannot bring the ordinary action at law for damages against the corporate directors for their negligence in the management of the corporate affairs.² It is clear also that the stock-

¹ See § 659, *supra*.

² The leading case on this point is *Smith v. Hurd*, 53 Mass. 371 (1847), the court saying: "An injury done to the stock and capital, by negligence or defea-

sance, is not an injury to such separate interest, but to the whole body of stockholders in common." *Brinckerhoff v. Bostwick*, 88 N. Y. 52 (1882), where the court say: "The cause of action set forth

holder cannot hold the corporation itself liable for the negligence herein of its directors. To allow such an action would be to make part of the stockholders liable to other stockholders for the loss, when all are equally injured, equally innocent, and equally in position to complain.¹ Ordinarily, the remedy for the negligence of corporate directors in the management of the corporate affairs, is an action at law instituted by the corporation itself. If, however, the corporation is under the control of the guilty parties, or if it refuses to sue, when requested by a stockholder to do so, then the stockholder himself may bring a suit in equity, in his own behalf, and in behalf of all other stockholders who may wish to come in, making the corporation, and the guilty parties, the defendants, and compel them to make good to the corporation the corporate money or property lost by their negligence. The money or property recovered in such an action belongs to the corporation, and not to the stockholder who brings the suit.² In a stockholder's suit to hold the directors liable for negligence, the acts of negligence need not be set out with great particularity. The suit is in a court of equity, and the court decides the questions of fact, since the suit is in the nature of an accounting.³

§ 680. *Instances of negligence of directors in the performance of their duties.*—It is difficult to lay down any rules as to what acts will constitute negligence on the part of corporate officers. Each case is to be determined largely on its own facts. Thus, where the directors kept no accounts, paid no calls, collect-

in the complaint are losses and misapplication of the funds of the bank through the negligence and misconduct of its directors. For these losses the bank, if still exercising its corporate functions, would have a claim upon the guilty directors which it could enforce by action; but if it refused to prosecute, or if it still remained under the control of the very directors against whom the action should be brought, the stockholders would have a standing in a court of equity to sue in their own names, making the corporation a party defendant." See also *Craig v. Gregg*, 83 Penn. St. 19 (1876). To same effect, *Allen v. Curtis*, 26 Conn. 456 (1857). "A fatal defect in the plaintiff's petition, both original and amended, is, that it seeks no recovery in behalf of the corporation, but seeks a direct re-

covery of damages for the plaintiff individually, the case stated not entitling him to such a recovery." *Evans v. Brandon*, 53 Texas, 56 (1880); *Kent v. Jackson*, 2 De G., M. & G. 49 (1852).

¹ *Oliphant v. Woodburn, &c. Co.*, 63 Iowa, 332 (1884).

² *Evans v. Brandon*, *supra*; *Dewing v. Perdicaris*, 96 U. S. 193, 198 (1877); *Smith v. Poor*, 40 Me. 415 (1855); *Carter v. Ford, &c. Co.*, 85 Ind. 180 (1882).

³ *Halsey v. Ackerman*, 38 N. J. Eq. 501 (1884), *aff'd* 10 Stew. Eq. 356. This case holds also that the stockholder's action lies, even after the corporation has become insolvent. See also *Smith v. Poor*, 3 Ware (U. S. C. C.), 148 (1858); *Gardiner v. Pollard*, 10 Bosw. (N. Y.) 674 (1863), and 11 N. Y. Rev. Stat. 589, § 1, and 591, § 16.

ed no subscriptions, they are quite properly held guilty of negligence, and may be made liable therefor.¹ So also the directors of a national bank are liable when they loan money to irresponsible persons, allow overdrafts, employ dishonest, unfaithful, and incompetent clerks, and neglect to take security from the cashier, president, and other officers, for good conduct and the performance of duties.² The president is negligent and is liable if he does not require the secretary to give a bond for his good conduct, as required by the by-laws of the corporation.³ But it has been held that the directors are not liable for a failure to have the secretary's bond renewed, they supposing that it did not expire at the end of the year.⁴ The law is well established that the corporate officers are not liable on the ground of negligence, for *ultra vires* acts which they have done or sanctioned, but in good faith and without knowledge of their *ultra vires* character. The act itself may be impeached and set aside, and property transferred thereunder may be recovered back, but if the directors have made an honest mistake, and it was a mistake which a man of usual intelligence might make, they are not personally liable therefor. The law does not require them to be learned in the law.⁵ The directors, however, are liable for allowing the treasurer to use corporate funds for lobbying purposes.⁶

§ 681. *Directors must use ordinary care and diligence in the management of the corporation and the transaction of its business.*—The directors of a corporation are not guarantors that no mistakes will be made in the management of the corporate business, nor do they insure the corporation against loss by the frauds or embezzlement of subordinate officers and agents. They are required to exercise reasonable care and sound business judgment, but nothing further than this. They generally serve without pay, and usually, by reason of their own interest in the

¹ Neall v. Hill, 16 Cal. 145 (1860).

² Brinkerhoff v. Bostwick, 88 N. Y., 52 (1882). See also Smith v. Rathbun, 22 Hun, 150 (1880).

³ Pontchartrain R. R. Co. v. Paulding, 11 La. 41 (1837).

⁴ Vance v. Phoenix Ins. Co., 4 Lea (Tenn.), 385.

⁵ Watt's Appeal, 78 Penn. St. 370 (1875), the court saying: "If while these men were acting honestly, and for what

they esteemed the best interests of the company, they were not willfully perverting their powers, but only misjudged the same, we cannot consent to compel them to account personally for the moneys thus expended." Hodges v. New Eng. Screw Co., 1 R. I., 312, 348 (1850). Cf. Joint Stock Co. v. Brown, L. R. 3 Eq. 139; 8 Eq. 381.

⁶ Shea v. Mabry, 1 Lea (Tenn.), 319 (1878).

stock of the company, are directly interested in the welfare of the corporation. But, though this is the case, they must use ordinary diligence in ascertaining the condition of things, and ordinary intelligence in their action as directors. They are liable for losses if they go to sleep at meetings of the directors, or if they regularly fail to attend such meetings.¹ They must exercise the same diligence and care that men of usual prudence and skill would exercise in the management of a similar business for them-

¹ The leading case on the liability of directors for negligence is *Charitable Corporation v. Sutton*, 2 Atk. 400 (1742), where Lord Chancellor Hardwicke said: "They may be guilty of acts of commission or omission, of *malfeasance* or *non-feasance*. Now, where acts are executed within their authority, . . . in such cases, though attended with bad consequences, it will be very difficult to determine that these are breaches of trust. For it is by no means just in a judge, after bad consequences have arisen from such executions of their power, to say that they foresaw at the time what must necessarily happen, and therefore were guilty of a breach of trust. Next as to *malfeasance* and *non-feasance*. To instance in non-attendance, if some persons are guilty of gross non-attendance, and leave the management entirely to others, they may be guilty by this means of the breaches of trust that are committed by others. By accepting of a trust of this sort, a person is obliged to execute it with fidelity and reasonable diligence, and it is no excuse to say that they had no benefit from it, but that it was merely honorary, and therefore they are within the case of common trustees." In *Percy v. Millaudon*, 6 Mart. La. 68 (1829), the court said: "If nothing has come to their knowledge, to awaken suspicion of the fidelity of the president and cashier, ordinary attention to the affairs of the institution is sufficient. If they become acquainted with any fact calculated to put prudent men on their guard, a degree of care commensurate with the evil to be avoided is required, and a want of that care certainly makes them responsible." This case also holds that directors are not liable for errors of judgment unless they are grossly wrong. In the case *United Society, &c. v. Underwood*, 9 Bush (Ky.), 609 (1873), the court said: "It is the duty of the board to exercise a general supervision over the affairs of

the bank, and to direct and control the action of its subordinate officers in all important transactions. The community have the right to assume that the directory does its duty, and to hold them personally liable for neglecting it." That the directors must use ordinary diligence, see *Williams v. Gregg*, 2 Strob. Eq. (S. C.) 297 (1848), and in *Richards v. New Hampshire Ins. Co.*, 43 N.H. 263 (1861), the court say: "The rule is a just one that an agent is bound to apply the same diligence to obtain payment of debts in his care that he does to recover his own." In the case *Land Credit Co. v. Fermoy*, L. R. 5 Ch. 763 (1870), where it was sought to hold liable for negligence, directors who innocently approved of a loan, which in reality had not been made, but the money had been used by other directors for speculative purposes, the court said: "I am exceedingly reluctant in any way to exonerate directors from performing their duty, and I quite agree that it is their duty to be awake, and that their being asleep would not exempt them from the consequences of not attending to the business of the company." In the case *Dunn's Adm'r v. Kyle's Adm'r*, 14 Bush (Ky.), 134 (1878), where a cashier had embezzled the funds of the bank, the court said: "Bad faith or gross negligence is certainly necessary to render the director liable to a stockholder in a case like this." The court also approved of the rule given in *Morse on Banking*, p. 117, to the effect that "for excusable mistakes concerning the law, and for many errors strictly of discretion, they are not liable. Though in cases in which their action has been so grossly ill-advised as to warrant the imputation of fraud, or to show a want of the knowledge absolutely necessary for the performance of their duties, so great that they were not justified in assuming the office, they may be held responsible."

selves. The directors are not bound to examine the books of the company, nor investigate the mode of living of their employees. But they are required to attend the directors' meetings with reasonable regularity; to have statements of the business made to them; to object to the transaction of important business without the knowledge and consent of the board of directors; to examine with reasonable care the reports and matters of business brought before them; and not to shut their eyes to obvious objections to the business transactions, and general condition of the corporation, or to the character and well known reputation of the employees.¹

¹ The law on this subject is ably and clearly set forth by Mr. Justice Earl, in *Hun v. Cary*, 82 N. Y. 65 (1880), as follows: "The trustees are bound to observe the limits placed upon their powers in the charter, and if they transcend such limits and cause damage, they incur liability. If they act fraudulently or do a willful wrong, it is not doubted that they may be held for all the damage they cause to the bank or its depositors. But if they act in good faith within the limits of powers conferred, using proper prudence and diligence, they are not responsible for mere mistakes or errors of judgment. That the trustees of such corporations are bound to use some diligence in the discharge of their duties cannot be disputed. All the authorities hold so. What degree of care and diligence are they bound to exercise? Not the highest degree, not such as a very vigilant or extremely careful person would exercise. If such were required, it would be difficult to find trustees who would incur the responsibility of such trust positions. It would not be proper to answer the question by saying the lowest degree. Few persons would be willing to deposit money in savings banks, or to take stock in corporations, with the understanding that the trustees or directors were bound only to exercise slight care, such as inattentive persons would give to their own business, in the management of the large and important interests committed to their hands. When one deposits money in a savings bank, or takes stock in a corporation, thus divesting himself of the immediate control of his property, he expects, and has the right to expect, that the trustees or directors, who are chosen to take his place in the management and control of his property, will exercise ordinary care

and prudence in the trusts committed to them—the same degree of care and prudence that men prompted by self-interest generally exercise in their own affairs. Where one voluntarily takes the position of trustee or director of a corporation, good faith, exact justice, and public policy unite in requiring of him such a degree of care and prudence, and it is a gross breach of duty—*crassa negligentia*—not to bestow them. It is impossible to give the measure of culpable negligence for all cases, as the degree of care required depends upon the subjects to which it is to be applied. . . . Like a mandatory, to whom he has been likened, he is bound not only to exercise proper care and diligence, but ordinary skill and judgment. As he is bound to exercise ordinary skill and judgment, he cannot set up that he did not possess them. Where damage is caused by his want of judgment, he cannot excuse himself by alleging his gross ignorance. One who voluntarily takes the position of director, and invites confidence in that relation, undertakes, like a mandatory, with those whom he represents or for whom he acts, that he possesses at least ordinary knowledge and skill, and that he will bring them to bear in the discharge of his duties. . . . Whether, under the circumstances, the purchase was such as the trustees, in the exercise of ordinary prudence, skill, and care, could make; or whether the act of purchase was reckless, rash, extravagant, showing a want of ordinary prudence, skill, and care, were questions for the jury." Cf. *Van Dyck v. McQuade*, 86 N. Y. 38 (1881). See also *Scott v. De Peyster*, 1 Edw. Ch. 513; *Litchfield v. White*, 3 Sandf. 545; *Liquidators, &c. v. Douglas*, 11 Sess. Cases, 3d series, 112; *Spering's Appeal*, 71 Penn. St. 11 (1872),

Moreover, when a director has knowledge that an unauthorized act is being done, he cannot escape liability, however innocent he may be, unless he prevents the act by his protest, or files a bill in equity to remedy the wrong.¹

an important case, and one which is frequently spoken of as the leading case herein. A director who trusts everything to the other directors, or who performs all acts as a mere man of straw, is liable. *Brown's Case*, L. R. 8 Eq. 404, 405. See also *Williams v. McKay*, 40 N. J. Eq. 189 (1885), where the court said in reference to the trustees of a savings bank, that they must manage "in the same way that men of common prudence and skill conduct a similar business for themselves.

. . . Doubtless such officers had the right to rely in many respects on the skill and diligence of their committeemen and if exercising a reasonable circumspection they were unaware of the misconduct or neglect of such agents, they would not be responsible for the consequences. But so plain was their duty to oversee the business done by such committeemen, that it seems to me, they are chargeable, *prima facie*, with a knowledge of what was doing, or had been done, in all important matters by such bodies." See also *Henry v. Jackson*, 37 Vt. 431; *Smith v. Prattville Manfg. Co.*, 29 Ala. 503; *Neall v. Hill*, 16 Cal. 145, 151. In the case *Ackerman v. Halsey*, 37 N. J. Eq. 356 (1883), *aff'd*, 38 Id. 501, the court said: "As a general rule, the directors of a corporation are only required in the management of its affairs to keep within the limits of its powers, and to exercise good faith

and honesty. They only undertake, by virtue of their assumption of the duties incumbent on them, to perform those duties according to the best of their judgment, and with reasonable diligence, and a mere error of judgment will not subject them to personal liability for its consequence. And unless there has been some violation of the charter or the constituting instruments of the company, or unless there is shown to be a want of good faith, or a willful abuse of discretion, there will be no personal liability. They are, personally, only bound in the management of the affairs of the corporation, to use reasonable diligence and prudence, such as men usually exercise in the management of their own affairs of similar nature. (Citing cases.) But they are personally liable if they suffer the corporate funds or property to be wasted by gross negligence or inattention to the duties of their trust." *Trustees, &c. v. Bosseux*, 3 Fed. Rep. 817 (1880).

¹ *Joint Stock Discount Co. v. Brown*, L. R. 8 Eq. 381, 402; *Ashhurst v. Fowler*, L. R. 20 Eq. 225. That a director is not in general liable for misdeeds of subordinate corporate agents, see *Bath v. Caton*, 37 Mich. 199; *Bachelor v. Pinkham*, 68 Me. 253; *Nicholson v. Mounsey*, 15 East, 384; *Stone v. Cartright*, 6 Term Rep. 411; *Hewitt v. Swift*, 3 Allen, 420. *Cf. Weir v. Barnett*, L. R. 3 Ex. D. 238.

CHAPTER XLI.

RATIFICATION, ACQUIESCENCE, OR LACHES AS A BAR TO A STOCKHOLDER'S ACTION HEREIN.

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| <p>§ 682. Introductory.</p> <p>683. Laches, acquiescence, or ratification as a defense to a stockholder's action to remedy <i>ultra vires</i> acts, which are prohibited by statute or contrary to public policy.</p> <p>684. Ratification herein may be express or implied.</p> | <p>§ 685. Stockholder chargeable with laches only after he has a full knowledge of the facts.</p> <p>686. Stockholder must sue within reasonable time after knowledge of the acts.</p> <p>687. Miscellaneous applications of the doctrine of laches herein.</p> |
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§ 682. *Introductory.*—When a stockholder brings an action to remedy the frauds, *ultra vires* acts, or negligence of a director or third person, the most common and dangerous defense that he has to encounter is the defense that he has been guilty of laches in bringing his action. Like the defense of contributory negligence, a modern principle of law that defeats many actions for negligence, so the defense of laches, acquiescence, or ratification, has sprung up to defeat stockholders' actions herein. The principles which govern, define, and explain this defense have become well settled. They form the subject of this chapter.

§ 683. *Laches, acquiescence, or ratification as a defense to a stockholder's action to remedy ultra vires acts, which are prohibited by statute or contrary to public policy.*—It has already been shown that a stockholder may bring an action to remedy frauds, negligence, or *ultra vires* acts. As regards the frauds and negligence of corporate officers it is well settled that laches is a good defense to a stockholder's action herein. But *ultra vires* acts are subject to a somewhat different rule. *Ultra vires* acts may be said to be of three kinds: first, acts which are unauthorized by statute and which are contrary to public policy, in other words, acts which are *mala in se*; second, acts which are prohibited by statute, such acts being *mala prohibita*; third, all other acts which are beyond the express or implied powers. As regards the last class, the defense of laches applies to a stockholder's action herein just the same as it applies to actions to remedy

a director's frauds or negligence. In reference to *ultra vires* acts, however, which are *mala prohibita* or *mala in se*, there is more difficulty. It is very clear that no assent or acquiescence of the stockholders can validate such acts.¹ But it is a different question to determine whether, after long acquiescence, the stockholder may take advantage of the invalidity of such acts. As regards acts *mala prohibita*, that is acts expressly prohibited by statute, it would seem that the stockholder may by his laches be barred from complaining thereof, since the State, through its attorney-general, may protect the interests of the public.² As regards acts *mala in se*, probably the rule will depend on the circumstances of the case. If the stockholder has participated in the act, or knowingly accepted the benefit thereof, the court will not aid him, since he who comes into equity must do so with clean hands.³ When, however, a stockholder has not participated or knowingly accepted the benefit of corporate contracts, which are *mala in se*, there would seem to be no reason why mere delay on his part in bringing suit to set aside such acts should be fatal to his bill.

§ 684. *Ratification herein may be express or implied.*—There are in general two ways in which a stockholder may be said to have ratified an act of the directors which he is attempting to enjoin or set aside. The ratification may be by an express agreement or statement to that effect, or it may be by such laches or acquiescence as will amount to an implied ratification.⁴ Cases

¹ See *Kent v. Quicksilver Min. Co.*, 78 N. Y. 159, 186 (1879), where the court says: "A corporation may do acts which affect the public to its harm, inasmuch as they are *per se* illegal or are *malum prohibitum*. Then no assent of stockholders can validate them."

² See *Stewart v. Erie, &c. Trans. Co.*, 17 Minn. 372 (1871); and in *Gray v. Chaplin*, 2 Russ. Ch. 126 (1826), the court said that the stockholder cannot claim that the public is wronged. "If a public right is to be enforced it must be at the suit of those to whom the protection of public rights belongs." Cf. *Ashbury Ry., &c. Co. v. Riche*, L. R. 7 H. of L. 653 (1875); *Taylor v. Chichester, &c. Ry. Co.*, L. R. 2 Ex. 356 (1867).

³ See § 39, *supra*.

⁴ Thus in *Evans v. Smallcombe*, L.

R. 3 H. of L. 249 (1868); aff'g L. R. 3 Eq. 769, the court said: "Consent might be either express or might be inferred from the acquiescence of the shareholders after full knowledge of the transaction which was in excess of the powers of the directors." In the case *Kent v. Quicksilver Min. Co.*, 78 N. Y. 159, 187 (1879), the court said: "Where third parties have dealt with the company, relying in good faith upon the existence of corporate authority to do an act, there it is not needed that there be an express assent thereto, on the part of the stockholders, to work an equitable estoppel upon them. Their conduct may have been such, though negative in character, as to be taken for an acquiescence in the act; and when harm would come to such third parties if the act were held invalid, the

involving the defense of an express ratification rarely arise since this defense is easy to prove. But the defense of an implied ratification is more difficult to establish. An implied ratification is generally spoken of as laches. It is the subject of the remainder of this chapter.¹

§ 685. *Stockholder chargeable with laches only after he has a full knowledge of the facts.*—Laches is a defense only when the stockholder with a full knowledge of the facts has delayed an unreasonable length of time in bringing his action. These two elements, knowledge and delay, are the essential elements of the defense.² Until the stockholder has full and complete knowledge

stockholders are estopped from questioning it. We suppose acquiescence or tacit assent to mean the neglect to promptly and actively condemn the unauthorized act and to seek judicial redress after knowledge of the committal of it, whereby innocent third parties have been led to put themselves in a position from which they cannot be taken without loss. It is the doctrine of equitable estoppel, which applies to members of corporate or associate bodies as well as to persons acting in a natural capacity."

¹ In the case *First Natl. Bk. v. Drake*, 29 Kan. 311 (1883): "But what is ratification? It is the confirmation of a voidable act. It is entirely immaterial what that is which renders the act voidable; whether a lack of present power to make a valid contract, as in the case of infancy, or because of fraud and misrepresentation on the part of the other contracting party, or because it is the unauthorized attempt of an assumed agent to bind his principal. Whenever there is a voidable act, confirmation of that act by the party assumed to be bound, is in law a ratification. But in order to constitute a valid ratification there must be knowledge."

² Thus in the leading case of *Cumberland Coal Co. v. Sherman*, 80 Barb. 538 (1859), the following from Lewin on Trusts is stated to be the law in relation to stockholders. 1. The confirming party must be *sui juris*, not laboring under any disability, as infancy or coverture. 2. The confirmation must be a solemn and deliberate act—not for instance fished out from some expressions in a letter; and particularly when the original transaction was infected with

fraud the confirmation of it is so inconsistent with justice and so likely to be accompanied with imposition that the court will watch it with the utmost strictness, and not allow it to stand but on the very clearest evidence. 3. There must be no *suppressio veri*, or *suggestio falsi*, but the *cestui que trust* must be honestly made acquainted with all the material circumstances of the case. 4. The confirming party must not be ignorant of the law; that is he must be aware that the transaction is of such a character that he could impeach it in a court of equity. 5. The confirmation must be wholly distinct from, and independent of, the original contract—not a conveyance of the estate, executed in pursuance of a covenant in the original deed for further assurance. 6. The confirmation must not be wrung from the *cestui que trust* by distress or terror. 7. When the *cestuis que trust* are a class of persons, as creditors, the sanction of the major part will not be obligatory on the rest; but the confirmation to be complete must be the joint act of the whole body." And in the equally important case *Hoffman, &c. Co. v. Cumberland, &c. Co.*, 16 Md. 456 (1860), the court said: "To render the act of ratification effective and conclusive certain considerations are necessary. At the time of the supposed ratification the principal must have been fully aware of every material circumstance of the transaction, the real value of the subject of the contract, and his act of ratification must have been an independent and substantive act, founded on complete information and of perfect freedom of volition, and, in addition to all this, the *cestui que trust* must not only have been acquainted

of all the essential facts which would be likely to induce him to institute the action, the beginning of the time from which laches will run cannot be said to commence.¹ Where, however, the facts are well known to all intelligent men, and the means of knowledge are open to the stockholder, he is chargeable with knowledge from the date when he should have ascertained the facts.²

But it is not incumbent on the stockholder to keep himself informed as to the various acts of the corporation. He is not chargeable with knowledge merely because he might have ascertained the facts by an examination of the corporate books.³ Moreover, it is the well established rule that lapse of time alone cannot support the defense of laches. There must be both knowledge and delay.⁴

§ 686. *Stockholder must sue within reasonable time after knowledge of the facts.*—After a stockholder has knowledge, or

with the facts, but apprised of the law, how these facts would be dealt with if brought before a court of equity."

¹In *Gilman, &c. R. R. Co. v. Kelly*, 77 Ill. 426 (1875), the court said: "No ratification will estop the principal unless he has been made aware of all the material facts and circumstances of the transaction that would in any way influence his mind or affect the value of the contract."

²*Taylor v. South, &c. R. R. Co.*, 4 Woods (U. S.), 575 (1882), the court saying: "The means of knowledge are the same thing in effect as knowledge itself. . . . The circumstances of the discovery must be fully stated and proved, and the delay which has occurred must be shown to be consistent with the requisite diligence." See also *Kelley v. Newburyport, &c. R. R. Co.* (Mass. 1886), 24 Am. & Eng. Ry. Cas. 27. In the case *Phosphate, &c. Co. v. Green*, L. R. 7 Com. Pl. 43 (1871), it was held that to show assent and acquiescence it is not necessary to prove the acquiescence of each individual shareholder. It is enough to show circumstances which are reasonably calculated to satisfy the court or a jury that the thing to be ratified came to the knowledge of all who chose to inquire, all having full opportunity and means of inquiry.

³*Stewart's Case*, L. R. 1 Ch. 511 (1866); *Stanhope's Case*, Id. 161, where the court said: "It is no part of the duty of a shareholder to look into the management of the business. . . . It is not enough to show that they might have become acquainted with the mismanagement of their affairs. It must be shown that they did so." See *Ryan v. Leavenworth, &c., Ry. Co.*, 21 Kan. 365 (1879). Also *Holmes v. Newcastle, &c., Co.*, 45 L. J. (Ch.) 383 (1876), holding that knowledge of a sale of property is not knowledge of an illegal dividend from the proceeds. See also *Spackman v. Evans*, L. R. 3 H. of L. 171 (1868). See also *Houldsworth v. Id.*, Id. 263.

⁴*Evans v. Smallcombe*, L. R. 3 H. of L. 249 (1868); aff'g L. R. 3 Eq. 769, the court saying: "Lapse of time alone certainly would not make valid that which, at the beginning, was invalid. . . . Length of time may, in many cases, materially assist in establishing the presumption of acquiescence in an act which requires a confirmation to give it validity. But then it is not time, but the acquiescence, which changes what would otherwise be a void act into a valid one." *Ashhurst's Appeal*, 60 Penn. St. 290 (1869), where, however, the court says that "acquiescence is presumed from delay."

is chargeable with knowledge, of an *ultra vires*, fraudulent, or negligent act of the directors, he must institute his suit, if at all, within a reasonable time thereafter.¹ As to what will constitute a reasonable time depends on the circumstances of the case. If it is evident that the stockholder is waiting to see whether the unauthorized act will be profitable to the corporation, the court will refuse to grant him any relief.² So also if the stockholder,

¹ In the case *Twin Lick Oil Co. v. Marbury*, 91 U. S. 587 (1875), Mr. Justice Miller gives a clear statement of the law herein. He says: "The doctrine is well settled that the option to avoid such a sale must be exercised within a reasonable time. This has never been held to be any determined number of days or years as applied to every case, like the Statute of Limitations, but must be decided in each case upon all the elements of it which affect that question. These are generally the presence or absence of the parties at the place of the transaction, their knowledge or ignorance of the sale, and of the facts which render it voidable, the permanent or fluctuating character of the subject-matter of the transaction as affecting its value, and the actual rise or fall of the property in value during the period within which this option might have been exercised. In fixing this period in any particular case, we are but little aided by the analogies of the Statutes of Limitation; while, though not falling exactly within the rule as to time for rescinding, or offering to rescind, a contract by one of the parties to it for actual fraud, the analogies are so strong as to give to this latter great force in the consideration of the case. In this class of cases the party is bound to act with reasonable diligence as soon as the fraud is discovered, or his right to rescind is gone. No delay for the purpose of enabling the defrauded party to speculate upon the chances which the future may give him of deciding profitably to himself, whether he will abide by his bargain or rescind it, is allowed in a court of equity." *Taylor v. South, &c., Ry. Co.*, 4 Woods (U. S.), 575 (1882), the court saying: "A stockholder of a corporation will not be allowed, after a reasonable time, to disturb and rescind a contract, made by his corporation, after the same has been fully executed, on the ground that it is *ultra vires* and in excess of the corporate powers granted by the charter of the corporation."

² Story's Eq. Jurisprudence, § 1539a; *Kitchen v. St. Louis, &c., Ry. Co.*, 69 Mo. 224 (1878), where the court said: "He has no right to lie idly by until new equities arise, and speculate on the success or non-success of the investment or transaction of which he complains, and see others, in good faith and without fraud, by a vast expenditure of money, make that valuable which was before valueless, and then come and ask the aid of the chancellor to enable him to appropriate to himself such benefits and advantages." In *Gregory v. Patchett*, 33 Beav. 595 (1864), the court said: "Shareholders cannot lie by sanctioning, or by their silence, at least acquiescing in an arrangement which is *ultra vires* of the company to which they belong, watching the result; if it be favorable and profitable to themselves to abide by it and insist on its validity, but if it prove unfavorable and disastrous, then to institute proceedings to set it aside." *Banks v. Judah*, 8 Conn. 145 (1830), where the court said: "Equity will not suffer a party to lie by till the event of the experiment shall enable him to make his selection with certainty of profit one way, and without loss any way." In the case *Watt's Appeal*, 78 Penn. St. 370 (1875), the court said: "When an act, done by directors, is in excess of their authority, yet has been done with the *bona fide* intent of benefiting the corporation which they represent, and a shareholder, knowing thereof, does not dissent within a reasonable time, his assent to the act will be presumed, and he will be estopped from gainsaying it. . . . When the act complained of is to be followed by a large expenditure of money, the shareholder should not only file his protest within a reasonable time, but should follow up the same by active preventive means. . . . He may not thus pocket the gain resulting from his delay, or thus wait in order to observe the result of the experiment, and when it fails to produce the result expected, fall back upon his

after a full knowledge of the facts, stands by and allows large operations to be completed, or money expended, or alterations to be made before he brings suit, he is guilty of laches, and his remedy is barred.¹ In like manner, where the stockholder, with full knowledge, has accepted the benefit of the act, he cannot complain thereafter.² And, in general, where it is clear that the stockholder had a full knowledge of all the essential facts of an act which he might bring a suit to remedy, but which, for an unreasonable length of time he fails to object to by a bill in equity, he will be held guilty of laches, and his right to institute the suit is barred.³

protest as a saving of his legal remedies." In *Sheldon v. Eickemeyer, &c., Co.*, 90 N. Y. 607 (1882), the court said: "The principal may, nevertheless, affirm the act, and a ratification is equivalent to a prior authorization. If all the stockholders of this corporation had, with full knowledge, subsequently ratified the transfer and affirmed the settlement, the act, though beyond the power given the trustees by the charter, could not subsequently be avoided by the stockholders or the corporation. . . . The party upon whose rights or interests a fraud is committed should not be allowed, after the facts come to his knowledge, to speculate upon the possible advantages to himself of confirming or repudiating the transaction. He must repudiate at once, and surrender his securities."

¹ "If, with knowledge of that fact, the shareholders remain a long time and take no step whatever; still more, if they so remain while great alterations are going on in the company, they must be taken to have retrospectively sanctioned what has been done." *Houldsworth v. Evans*, L. R. 3 H. of L. 263, 276 (1868). "Where the summary interference of this court is invoked in cases of this nature, it must be invoked promptly. Parties who have lain by and permitted a large expenditure to be made, in contravention of the rights for which they contend, cannot call upon this court for its summary interference. . . . The weight which is due to lapse of time must, as I apprehend, in a great measure, depend upon the extent of the expenditure." *Delay of eight months held fatal. Great Western Ry. Co. v. Oxford, &c., Ry. Co.*, 3 De G., M. & G. 341 (1853). See also *Boston, &c., R. R. Co. v. N. Y. & N. E. R.*

R. Co., 13 R. I. 260 (1881); *Aurora, &c., Soc. v. Paddock*, 80 Ill. 263 (1875); *Stewart v. Erie, &c., Trans. Co.*, 17 Minn. 372 (1871), where the court said: "If a stockholder assents to acts *ultra vires*, or although not originally or expressly assenting, has for an unreasonable time acquiesced, and has permitted them to go unquestioned, so that other parties who have acted upon the faith of them (as, for instance, by making large expenditures of money), would suffer great injury from their repudiation, a court of equity would not easily be induced to grant relief at the instance of such stockholder." *Goodin v. Cincinnati, &c., R. R. Co.*, 18 O. St. 150 (1868). In the well-considered case, however, of *Covington, &c., R. R. Co. v. Bowler's Ex'rs*, 9 Bush, 570, the court held that a delay of six years was not a bar to the stockholder's remedy, and the court said that "merely remaining passive does not deprive a party of the right to seek redress, unless, in addition thereto, he does some act to induce or encourage others to expend their money or to alter their conditions, and thereby render it unconscientious for him to enforce his rights."

² "When a purchaser has taken possession of and enjoyed the subject-matter of a contract, it is, in my opinion, the duty of this court to make every reasonable presumption in favor of the validity of the contract." *London Assurance Co.'s Case*, 5 De G., M. & G. 465, 481 (1854). See also *Weed v. Little Falls, &c., Co.*, 31 Minn. 154 (1883).

³ *Spackman v. Evans*, L. R. 3 H. L. 171 (1868); *Downes v. Ship*, Id. 343; *Ashhurst's Appeal*, 60 Penn. St. 290 (1869); *Zabriskie v. Hackensack, &c., R. R. Co.*, 18 N. J. Eq. 178 (1867); *Mc-*

There has been considerable doubt and difficulty in determining whether the Statute of Limitations will be applied by a court of equity to cases of this nature. It has been held in England that the statute will be applied to a corporate action to compel a director to pay over to the corporation money received by him as a bribe, and that the statute begins to run from the time when the corporation discovers the facts.¹ And a similar rule seems to prevail in Pennsylvania.²

§ 687. *Miscellaneous applications of the doctrine of laches herein.*—It is well settled that the ratification of an act which the stockholder might have complained of does not authorize or ratify in advance a repetition of that act.³ A stockholder's right

Loughlin v. Detroit, &c., Ry. Co., 8 Mich. 100 (1860); *Gray v. Chaplin*, 2 Russ. Ch. 126 (1826), where the stockholder had acquiesced 47 years in an *ultra vires* lease. In the case *Mills v. Central R. R. Co.*, 41 N. J. Eq. 6 (1886), it was very properly held that a delay of 54 days was no bar, and also that a failure to vote against the act was no bar. In the case *Gifford v. N. J. R. R. Co.*, 10 N. J. Eq. 171 (1854), a delay of 20 years was held to be a bar. In the following cases the court held delay to be a bar: *Peabody v. Flint*, 88 Mass. 54 (1863), the delay being three and one-half years. *Gregory v. Patchett*, 33 Beav. 595 (1864), six years; *International, &c., R. R. Co. v. Bremond*, 53 Tex. 96 (1880), two years; *Graham v. Birkenhead, &c., Co.*, 2 Mac. & G. 146 (1850), eighteen months; *Kitchen v. St. Louis, &c., Ry. Co.*, 69 Mo. 224 (1878), two years; *Boston, &c., R. R. Co. v. N. Y. & N. E. R. R. Co.*, 13 R. I. 260 (1881); *Ashhurst's Appeal*, 60 Penn. St. 290 (1869), seven years; *Sheldon, &c., Co. v. Eickemeyer, &c., Co.*, 90 N.Y. 807 (1882), four years; *Pneumatic Gas Co. v. Berry*, 113 U. S. 322 (1884); *Graham v. Boston, &c., R. R. Co.*, 118 U. S. 161 (1886); *In re Pinto Silver Min. Co.*, L. R. 8 Ch. D. 273; *Royal Bk. of Liverpool v. Grand Junction R. R. Co.*, 125 Mass. 490 (1878); *In re Magdalena, &c., Co.*, 6 Jur. N. S. 975 (1884), where a delay of two years was held a bar; *Brotherhood's Case*, 31 Beav. 365 (1862), twelve years; *Hervey v. Illinois, &c., Ry. Co.*, 28 Fed. Rep. 169 (1884); *Thompson v. Lambert*, 44 Iowa, 239 (1876); *Vigers v. Pike*, 8 Cl. & Fin. 562, 650 (1840); *Zabriskie v. Cleveland, &c., R. R. Co.*, 23 How. 381

(1859). Cf. *Boardman v. Lake Shore, &c., Ry. Co.*, 84 N. Y. 157 (1881); *Badger v. Badger*, 2 Wall. 87; *Harwood v. Railroad Co.*, 17 Wall. 78; *Rochdale Canal Co. v. King*, 2 Sim. N. S. 89; §§ 161, 162, 198, *supra*.

¹ *Metropolitan Bk. v. Heiron*, L. R. 5 Ex. D. 319 (1880). *Contra*, *Ernest v. Croysdill*, 2 De G., F. & J. 175 (1860).

² *Watts' Appeal*, 78 Penn. St. 370 (1875). See also *Taylor v. South, &c., R. R. Co.*, 4 Woods, 575 (1882). Also in California. See *Dannmeyer v. Coleman*, 11 Fed. Rep. 99 (1882), holding that the three years' limitation to actions based on fraud, after discovery thereof, applies to directors' frauds herein. But see *Philippi v. Philippi*, 115 U. S. 151. See in general, *Coit v. Campbell*, 82 N. Y. 509, 514; *Farnam v. Brooks*, 9 Pick. 242; *Godden v. Kimmell*, 99 U. S. 201, 210; *Preston v. Preston*, 95 U. S. 200; *Badger v. Badger*, 2 Wall. 87; *Medder v. Norton*, 11 Wall. 442; *Bowman v. Wathen*, 1 How. 188; *Beckford v. Wade*, 17 Ves. 87.

³ *Irvine v. Union Bank of Australia*, 37 L. T. N. S. 176 (1877); s. c., L. R. 2 App. 366; *Bloxham v. Metropolitan Ry. Co.*, L. R. 3 Ch. 337, 354 (1868), where the court said: "If the acts of the directors were positively illegal, the fact of knowing them, or even of deriving benefit from them, would not have prevented the original holder of the stock from afterwards objecting to similar acts. But it never can be held that the acquiescence of the original holder of stock in illegal acts of the directors of a company will bind a subsequent holder of that stock to submission to all future acts of the same character."

to object to a director's act can be exercised by him alone.¹ It is also well established that the ratification which will bind a stockholder must be by himself alone. It cannot be by the other stockholders.² But the acquiescence of a stockholder bars an action by any transferee of that stock.³

¹ *Taylor v. Chichester, &c., R. Co., L. R. 2 Ex. 356, 378 (1867)*, where the court said: "But the shareholder may waive any right which is given to him for his own protection only; and if he has either expressly or tacitly done so, he can no longer object. And neither a stranger, nor the body corporate itself, can raise such an objection to a contract made by the corporation if no shareholders choose to raise it for themselves."

² *Hazard v. Durant*, 11 R. I. 195 (1875). This principle of law is substantially a mere restatement of the principle that the majority cannot bind the minority as regard *ultra vires* acts; nor can the directors. See *Gallery v. Natl. Ex. Bk.*, 41 Mich. 169 (1879); Green's *Brice's Ultra Vires*, 2d ed. 675.

³ *Flooks v. South, &c., Ry. Co.*, 1 Sim. & G. 142 (1855).

CHAPTER XLII.

PARTIES, PLEADINGS, AND REMEDIES.

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| <p>§ 688. Jurisdiction of the court.</p> <p>689. Parties plaintiff.—Who may bring the suit.</p> <p>690. Rule when the plaintiff stockholder sues in the interest of a rival company, or purchased his stock for the purpose of bringing suit.</p> <p>691. The complainant stockholder must sue in behalf of himself and other stockholders.</p> <p>692. Parties defendant herein.</p> <p>693. Complainant's bill must not improperly join two or more causes of action herein.</p> <p>694. Complainant must allege that he requested the corporation to bring the suit, and that the corporation refused or neglected to do so.</p> | <p>§ 695. When such an allegation may be omitted.</p> <p>696. Miscellaneous allegations of the complainant.</p> <p>697. Prayer for relief.</p> <p>698. Property received under the act objected to must be returned upon that act being set aside.</p> <p>699. Injunction restraining the corporate officers and others from doing specified acts.</p> <p>700. Injunction against corporate officers acting at all, and the appointment of a receiver.</p> <p>701. Miscellaneous remedies.</p> <p>702. The complaining stockholder controls the conduct of the suit.</p> <p>703. No contribution among the directors.</p> |
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§ 688. *Jurisdiction of the court.*—There has been some difficulty in determining whether the Federal courts have jurisdiction of a stockholder's suit herein, when the corporation and the directors are citizens of one State, and the complainant stockholder is a resident of another State. Inasmuch as the suit is for the benefit of the corporation, it has been claimed that the non-residence of the stockholder is insufficient to give jurisdiction. The Federal courts have decided, however, that such jurisdiction exists, and it is in these courts that a large proportion of these suits are brought.¹ It is also a rule of law, that the courts of one State will not, at the suit of a stockholder, enjoin or set aside acts of a foreign corporation, since there is no method of enforcing the decree of

¹ Dodge v. Woolsey, 18 How. 331; Pond v. Vt. Valley R. R. Co., 12 Blatch. 280 (1874), the court holding also that the complainant might omit as party plaintiff, a stockholder residing in the State of the corporation. See also Hatch v. Chicago, &c., R. R. Co., 6 Blatch. 105 (1868); Bell v. Donohue, 17 Fed. Rep. 710 (1883), holding that the court has no

jurisdiction if the stockholder and the corporation are citizens of the same State. Cf. La Grange v. State Treas., 24 Mich. 468 (1872). In Hawes v. Oakland, 104 U. S. 450 (1881), the court vigorously denounced transfers of stock made for the purpose of giving the Federal courts jurisdiction. The 94th Rule was made in consequence thereof.

the court.¹ Moreover, the stockholder's suit herein must always be brought in a court of equity. It is never in a court of law.²

§ 689. *Parties plaintiff.*—Who may bring the suit.—Ordinarily, a suit herein is instituted by one or more stockholders who are registered as such on the corporate books. It has been held, however, that the suit may be brought by a purchaser of a certificate of stock who has not as yet obtained a registry thereof.³ The suit brought by one or more stockholders herein must be in behalf of themselves and such other stockholders as may wish to come in. Care is to be exercised, however, that stockholders, who are disqualified from participating in the suit, should not be joined as parties plaintiff.⁴ It is doubtful whether a corporate creditor may maintain a suit herein, to compel the corporate directors to account for their frauds, negligence, or *ultra vires* acts. The later rule seems to hold that such a suit will lie.⁵ Moreover, it has been held where a person, who holds stock as a trustee, refuses to bring the suit, that the *cestui que trust* may institute it, making the trustee a

¹ Williston v. Michigan, &c., R. R. Co., 95 Mass. 400 (1866); Howell v. Chicago, &c., Ry. Co., 51 Barb. 378 (1867); Gregory v. N. Y., &c., R. R. Co., 40 N. J. Eq. 38 (1885), where a resident stockholder in a foreign corporation sought to set aside its lease to a resident corporation; Cunningham v. Pell, 5 Paige, 607 (1836), holding that no personal judgment could be rendered against an absent director who was not personally served. In the case Ervine v. Oregon, &c., Co., 62 How. Pr. 490 (1882), the court sustained the jurisdiction where service on the directors was personal, even though the corporate property was not in the State. The court said: "The relief within the power of the court to grant may be incomplete, and not commensurate with the injuries and loss sustained, growing out of the fact that material interests affected are outside of this jurisdiction; but that affords no adequate reason why an attempt in that direction should not be made. Efforts in such direction frequently afford only approximate justice."

² See Gardiner v. Pollard, 10 Bosw. 674 (1863); Craig v. Gregg, 83 Penn. St. 19 (1876), and see § 679, *supra*. This principle of law is assumed in nearly all the cases cited in Part IV of this work.

³ Bagshaw v. Eastern Union Ry. Co.,

7 Hare, 114 (1849); Ervine v. Oregon, &c., Co., 62 How. Pr. 490 (1882); Parrott v. Byers, 40 Cal. 614 (1871). Cf. Landes v. Globe, &c., Co., 73 Ga. 176 (1884), where a stockholder had not paid his subscription. *Contra*, Ramsey v. Erie Ry. Co., 7 Abb. Pr. (N. S.) 156 (1869); Heath v. Erie Ry. Co., 8 Blatchf. 347 (1871); Hersey v. Veazie, 24 Me. 9 (1844).

⁴ Clements v. Bower, 1 Drew. 684 (1853). Cf. Parrott v. Byers, *supra*, holding that if one of the complainants is competent, it is immaterial that the others are not. See also Burt v. British, &c., Assn. 4 De G. & J. 158 (1859), where the court said that if the stockholders "sue by a plaintiff who is personally precluded from suing the suit cannot proceed."

⁵ Warner v. Hopkins, 111 Penn. St. 328 (1885); Lothrop v. Stedman, 42 Conn. 583 (U. S. C. C. 1875); Brown v. Orr, 3 Atl. Rep. 815 (Penn. 1886); but see Balliet v. Brown, 103 Penn. St. 546 (1883); Mills v. Northern Ry., &c., Co., L. R., 5 Ch. 621 (1870); Gavenstein's Appeal, 49 Penn. St. 310 (1865); Heath v. Erie Ry. Co., 8 Blatchf. 347 (1871); Currier v. N. Y., &c., R. R. Co., 35 Hun, 355 (1885). Cf. Van Weel v. Winston, 115 U. S. 228.

party defendant.¹ When some of the complainants are prosecuting the same cause of action elsewhere, the suit will be dismissed.²

§ 690. *Rule when the plaintiff stockholder sues in the interest of a rival company, or purchased his stock for the purpose of bringing suit.*—The law is well settled, that if a stockholder institutes a suit in behalf of himself and other stockholders, to enjoin or to bring to an accounting the corporate directors, and such suit is instituted, not to protect and benefit the stockholders' interest in the corporation, but to benefit some other corporation, the court will refuse to entertain the suit and will dismiss it.³

¹ Great Western Ry. Co. v. Rushout, 5 De G. & Sm. 290 (1852).

² Black v. Huggins, 2 Tenn. Ch. 780 (1877). See also as to who may be a complainant herein, Green's Brice's Ultra Vires, 2d ed., 649. In the case Dannmeyer v. Coleman, 11 Fed. Rep. 97 (1882), the court queries whether each stockholder may institute a separate suit herein.

³ The difficulty herein is in proving that the complainant is suing for the rival company. If, however, the latter is paying the costs of the suit, that is sufficient proof. Forrest v. Manchester, &c., Ry. Co., 4 De G., F. & J. 126 (1861), where the court said: "The principle upon which the constructive representation of the shareholders is permitted, indisputably requires that the suit shall be a *bona fide* one, faithfully, truthfully, sincerely directed to the benefit and the interests of these shareholders whom the plaintiff claims a right to represent." The court will not permit "a man who is the puppet of another company to represent the shareholders of the company against whom he desires to establish the interests and benefits of a rival scheme. That would be entirely contrary to the principle upon which this constructive representation has been permitted to be founded." There is a wide difference between this suit, which "directed, and a suit which is *bona fide* instituted by the plaintiff, persuaded only to the institution of it by the arguments of another company. . . . The motives of plaintiffs have nothing to do with the litigation. But an acknowledgment that the suit is brought for others makes it 'an imposition on the court.'" To same ef-

fect Belmont v. Erie Ry. Co., 52 Barb. 637 (1869). See also Felder v. London, &c., Ry. Co., 1 Hem. & M. 489 (1863), where the court said: "To entitle a shareholder to maintain a suit of this nature, the risk and responsibility must be upon him, so that the court can feel that he is acting for the benefit, or what he believes to be the benefit of the company. . . . What the court looks at is this, is the suit *bona fide* the plaintiff's own suit, or is he merely the hand by which some one else acts? And there is no ingredient entitled to greater weight in arriving at a conclusion on this point than the question, who is responsible for the costs of the suit?" To same effect see Camblos v. Phil., &c., R. R. Co., 4 Brews. 563 (U. S. C. C. 1873); Waterbury v. Merchants, &c., Ex. Co., 50 Barb. 157 (1867); s. c. 3 Abb. Pr. (N. S.) 163; Rogers v. Oxford, &c., Ry. Co., 2 De G. & J. 662 (1858). See, however, Densmore v. Central R. R. Co., 19 Fed. Rep. 153 (1883), holding that the fact that the complainant stockholder has business relations with the rival company, and is aided by it in preparing his case, is no bar, and that if it were, the objection is to be raised by a plea in abatement. In the case Ffooks v. Southwestern Ry. Co., 1 Sm. & G. 142 (1853), the court said: "Where the fact is established that, under the pretense of serving the interests of one company, the shareholders in a rival company, by purchasing shares for the purpose of litigation, can make this court the instrument of defeating or injuring the company into which they so intrude themselves, in order to raise questions and disputes on matters as to which all the other members of the company may be agreed, I

The application of a stockholder herein to a court of equity will not be denied merely because it is for the interest of the public, or of the corporation, or of the stockholder himself, that the act complained of be allowed to stand. The law does not depend upon the opinion of the court as to the benefit of the act.¹

In regard to purchases of stock for the very purpose of bringing a stockholder's suit herein, there is some difference of opinion. The common law clearly is that such a stockholder has the same right to bring the suit that his transferrer had.² Such is the rule even though the stock was purchased for the purpose of bringing the suit. The law has nothing to do with the motive of a legal act.³

cannot consider that in such a case it is the province of this court ordinarily to interfere."

¹ *Hoole v. Great, &c., Ry. Co., L. R., 3 Ch. 262 (1867); Stevens v. Rutland, &c., R. R. Co., 29 Vt. 545 (1851)*, where the court said: "In regard to the expediency of bringing this bill, the chancellor cannot and has no right to judge. The orator has the constitutional and sole right of determining this matter; and if he thinks it expedient, we must acquiesce in it; and no plea of the public good or inequality of interests involved can justify the chancellor in denying to the orator a right which is clearly accorded to him by well established chancery principles."

² *Winsor v. Bailey, 55 N. H. 218 (1875)*, the court so holding and saying that to hold otherwise "would seem to involve the singular consequence that the transfer of stock in a corporation extinguishes the right to inquire into the previous fraudulent conduct of its officers, whereby its funds have been misappropriated. . . . The transfer of the stock conveyed to them, not only the ownership of the shares and the right to the future dividends thereon, but also placed them on an equal footing with the other stockholders in respect to the right to call the officers and agents of the corporation to an account for their fraudulent conduct." To same effect see *Bloxam v. Metropolitan Ry. Co., L. R., 3 Ch. 337 (1868)*, where the complainant on December 13, 1867, advertised to induce the stockholders to combine; on January 13, 1868, purchased stock himself, and on January 25, 1868, commenced suit. So also see *Seaton v. Grant, L. R., 2 Ch. 459*

(1867), where the court sustained the suit, although it said: "He buys five shares in the company, and then files his bill, in order to induce the company to buy off the litigation. That, no doubt, is a course of conduct which would meet with little approval in this court, or, indeed, in any other court, and such conduct might be material at the hearing, with reference to the amount of relief which the plaintiff could obtain or whether he was entitled to any relief at all." Nevertheless the court said also that "however questionable the mode of the plaintiff's introduction to the company may have been, he has an actual interest in the subject-matter of the suit." In the case *Du Pont v. Northern Pac. R. R. Co., 18 Fed. Rep. 467 (1883)*, Judge Wallace said: "A court of equity will not be swift to grant the stringent relief of a preliminary injunction to an officious plaintiff who seems to have acquired his interests as a stockholder with a view of assailing transactions in the corporate affairs of which existing stockholders do not seem to have complained."

³ Cases, *supra*, also *Elkins v. Camden, &c., R. R. Co., 36 N. J. Eq. 5 (1882); Ramsey v. Gould, 57 Barb. 398 (1870)*, where the court said: "The court has no right to look into the plaintiff's motive in bringing it; and, although, in moving it, his malice is gratified, or his independent litigations incidentally subverted, still, unless the court can plainly see that he has no meritorious cause of action, or that he is estopped from prosecuting it, his prosecution of it will not be deemed a perversion or abuse of the process of the court. This is equally true in a court of equity, as in a court of law.

But where the transfer is merely nominal, the transferee cannot bring suit herein, since he has no pecuniary interests of his own to protect, and equity will not aid him.¹ The smallness of this stockholder's interest, however, will not prevent his instituting a stockholder's suit to remedy a corporate wrong. An owner of one share is to be protected by a court of justice equally with the owner of a thousand shares. The old doctrine of *de minimis non curat lex*, has sometimes been applied to this class of cases, but such decisions are not to be commended. If there are no suspicious circumstances connected with the suit, it is believed that this maxim of the law will not be applied to a case of this character.²

In the Federal courts different rules prevail. It was found that transfers of stock were frequently made for the purpose of securing jurisdictions of the case in the Federal courts. Liti-

. . . The intent with which he purchased does not change or affect these rights, or raise any equities respecting them, in favor of the defendants."

¹ *M'Donnell v. Grand Canal Co.*, 3 Ir. Ch. Rep. N. S. 578 (1853), the court saying, "The petitioners, with full knowledge of the transaction, for the purpose of intervening in a concern in which they had no property, and preventing this transaction, got transferred to them shares for a nominal consideration, for the purpose of filing this petition just when the transaction was about to be completed. This court is not to be made the instrument of such a proceeding." See also *Robson v. Dodds*, L. R., 8 Eq. 302 (1869).

² *Armstrong v. Church Society*, 13 Grant Ch. (U. C.) 552 (1867), the court saying, "Every member of a corporation has a right to object to any illegal diversions of its funds; and in this respect those who contribute most have no greater rights than those who contribute least." *Seaton v. Grant*, L. R., 2 Ch. 459 (1867), where the court said, the maxim did not apply since the stockholder sued, not on his own behalf alone, but for himself and others. However, in the case of *Dannemeyer v. Coleman*, 11 Fed. Rep. 97 (1882) the court said, "It is always a

suspicious circumstance where a single stockholder, among a large number in a corporation, rushes into a court of equity to vindicate, unaided and alone, the rights of the corporation and all other stockholders; and especially is this so where the amount of stock owned by him is so very limited that in case of success his own share of the recovery will be so small as to make the maxim *de minimis non curat lex* very properly applicable." *Cf. Ithaca, &c., Co. v. Treman*, 93 N. Y. 660 (1883). In the case of *Charlton v. Newcastle, &c., Ry. Co.*, 5 Jur. N. S. 1096 (1859), the court said, "A single shareholder, holding five or ten shares or less, is perfectly justified in applying to the court to restrain a company, on behalf of himself, and the other shareholders by injunction, from committing any illegal act, beyond their powers. It does not signify if all the other shareholders are pitted together against this holder of ten shares, the court holds it is better for the real interests of the company that they should obey the law, and any one single shareholder who invokes the aid of the court is entitled to its aid for that purpose."

³ See the vigorous denunciation of such transfers by Mr Justice Miller, in *Hawes v. Oakland*, 104 U. S. 450 (1881).

cannot sustain a stockholder's suit to remedy a corporate wrong which was perpetrated before he became a stockholder.¹

§ 691. *The complainant stockholder must sue in behalf of himself and other stockholders.*—It is a well established rule of law that a stockholder's suit to remedy a wrong done to the corporation must be in behalf of all the stockholders, since they are all equally interested in the results of the suit. Accordingly the complainant or complainants must bring the suit in behalf of themselves, and such others of the stockholders as care to come in.² If all the stockholders, however, are made parties, there is no need of the suit being brought in behalf of others who may choose to come in.³

§ 692. *Parties defendant herein.*—The corporation itself is an indispensable party defendant to a stockholder's action for the purpose of remedying a wrong which the corporation itself should have remedied.⁴ This rule is due to the fact that all other pos-

¹ Rule 94, as follows: "Every bill brought by one or more stockholders in a corporation, against the corporation, and other parties, founded on rights which may properly be asserted by the corporation, must be verified by oath, and must contain an allegation that the plaintiff was a shareholder at the time of the transaction of which he complains, or that his share had devolved on him since by operation of law, and that the suit is not a collusive one to confer on a court of the United States jurisdiction of a case of which it would not otherwise have cognizance." Promulgated, January 23, 1882. See *Dimpfel v. Ohio, &c., R. R. Co.*, 110 U. S. 209 (1884). But see *Leo v. Union Pacific Ry. Co.*, 17 Fed. Rep. 273 (1883). In *Lafayette Co. v. Neely*, 21 Fed. Rep. 738 (1884), it is held that this rule does not bar the stockholders' right to bring the action after a dissolution of the corporation. See also *Whittemore v. Amoskeag Natl. Bk.*, 26 Fed. Rep. 819 (1885).

² *Wallworth v. Holt*, 4 Mylne & C., 619 (1840); *Taylor v. Solomon*, Id. 134 (1838), on the ground "that where the parties interested are numerous, and the suit is for an object common to them all, some of the body may maintain a bill on behalf of themselves and of the others is established." *Beman v. Rufford*, 1 Sim.

N. S. 550 (1851); *Baldwin v. Lawrence*, 2 Sim. & Stu. 18 (1824); *Bromley v. Smith*, 1 Sim. 8 (1826); *White v. Carmarthen, &c., Ry. Co.*, 1 Hem. & M. 786 (1863); *Bailey v. Birkenhead, &c., Ry. Co.*, 12 Beav. 433 (1850); *Preston v. Grand Collier Dock Co.*, 11 Sim. 327 (1840); *Winsor v. Bailey*, 55 N. H. 218 (1875); *Blatchford v. Ross*, 54 Barb. 42 (1869); *Cunningham v. Pell*, 5 Paige, 607 (1836); *Fawcett v. Laurie*, 1 Dr. & Sm. 192 (1860); *March v. Eastern R. R. Co.*, 40 N. H. 548 (1860); *Whitney v. Mayo*, 15 Ill. 251 (1853). But see *Cass v. Ottawa, &c., Co.*, 22 Grant (U. C.), 512 (1875); and *Hoole v. Great Western Ry. Co., L. R.*, 3 Ch. 262 (1867), to the effect that the rule is otherwise as regards *ultra vires* acts.

³ *Rogers v. Lafayette Agri. Works*, 52 Ind. 295 (1875). *Of. Bengley v. Wheeler*, 45 Mich. 493 (1881).

⁴ *Davenport v. Dows*, 18 Wall. 626 (1873); *Coxe v. Hart*, 53 Mich. 557 (1884); *Black v. Huggins*, 2 Tenn. Ch. 780 (1877); *Samuel v. Halladay*, 1 Woolw. 600 (1869); *Allen v. N. J. Southern R. R. Co.*, 49 How. Pr. 14 (1875); *Bagshaw v. Eastern, &c., Ry. Co.*, 7 Hare, 114 (1849); *Gregory v. Patchett*, 33 Beav. 595 (1864); *Charleston, &c., Co. v. Sebring*, 4 Rich. Eq. (S. C.) 342 (1853); *Brinckerhoff v. Bostwick*,

sible future suits by the corporation are thereby prevented, the rights of the corporation are duly ascertained, and the remedy made effectual against the corporation as well as others. It is not necessary nor proper to join the directors of the corporation as parties defendant where the only object of the suit is to enjoin an act or to set aside an *ultra vires* act. The decree against the corporation is effective and binding upon all the officers of the corporation.¹ Where, however, the object of the suit is to hold the directors personally liable for frauds or for negligence, the rule is different. In such cases they, of course, are necessary parties defendant.² As regards outside parties they are to be joined as parties defendant whenever the relief asked would affect their rights.³

§ 693. *Complainant's bill must not improperly join two or more causes of action herein.*—If the complainant's bill is multifarious it, of course, cannot succeed as against the objection of the defendants. Thus it has been held that the stockholders cannot join an action in reference to dividends with one for an injunction to restrain the corporate business from committing a

88 N. Y. 52 (1882); *Cunningham v. Pell*, 5 Paige, 607 (1836).

¹ *Winch v. Birkenhead, &c., Ry. Co.*, 5 De G. & Sm. 562 (1852), where the court said, "I do not think it is necessary that the directors should be parties. The act that is sought to be restrained is the act of the company. The company itself cannot act except by means of its officers." *Pioneer Gold, &c., Co. v. Baker*, 20 Fed. Rep. 4 (1884); *Heath v. Erie Ry. Co.*, 8 Blatch. 347 (1871); *Bryson v. Warwick, &c., Co.*, 1 Sm. & G. 447 (1853); *Bagshaw v. Eastern, &c., Ry. Co.*, 7 Hare, 114 (1849); *Allen v. N. J. Southern R. R. Co.*, 49 How. Pr. 14 (1875), the court saying, "They are represented by the corporation of which they are alleged to be directors, and when the corporation itself is made a party defendant it is improper to add the trustees or directors as parties when no personal claim or judgment is asked against them." But see *Ribon v. Railroad Cos.*, 16 Wall. 446 (1872).

² See cases in Chapter XXXIX, and Chapter XL, "C;" *Ducket v. Gover*, L. R., 6 Ch. D. 82; *Mason v. Harris*, L. R., 11 Ch. D. 97 (1879).

³ *Russell v. Wakefield, &c., Co.*, L. R.,

20 Eq. 474, the court saying, "When you have got the second corporation or person a party to the suit, it may happen that in addition to the relief that you are entitled to as regards the first, you are entitled to have relief against the second for something that has been done under the *ultra vires* agreement. You may be entitled to have money paid back which has been paid under the *ultra vires* agreement . . . and you may be entitled to have property returned or other acts done." * *Hare v. London, &c., Ry. Co.*, 1 John. & H. 252 (1860), holding that in an action to set aside a traffic contract, all the corporations who were parties to the contract are necessary parties. *Tyson v. Mahone*, 1 Hughes (U. S. C. Ct.), 80 (1871), to the effect that, in an action to set aside a consolidation, the other corporation is a necessary party. *Bill v. Donohue*, 17 Fed. Rep. 710 (1883); *Abbot v. American Hard Rubber Co.*, 4 Blatch. 489 (1861); *Bengley v. Wheeler*, 45 Mich. 493 (1881); *Shawhan v. Zinn*, 79 Ky. 300 (1881), holding that the objection to a defect of parties herein may be raised at the trial, and need not be raised by demurrer. *Cass v. Ottawa, &c., Co.*, 22 Grant (U. C.), 512 (1876),

fraud.¹ A bill combining an action to restrain the corporation from investing in the stock of another company, and one to restrain it from aiding that company, has been held to be multifarious.² The stockholders cannot join a suit against the corporation, with one against third persons in behalf of the corporation.³

§ 694. *Complainant must allege that he requested the corporation to bring the suit, and that the corporation refused or neglected to do so.*—Inasmuch as a fraud, *ultra vires* or negligent act of the directors of a corporation is an injury done to the corporation itself, it is the duty and proper function of the corporation to institute any action that may be brought to remedy the injury to the corporation. As already explained, however, a stockholder may bring the action if the corporation improperly refuses or neglects to institute such suit. Before the stockholder brings suit he must make a formal request to the corporate officers that suit be instituted by the corporation. Upon its refusal or neglect to comply with that request he may then bring suit himself. It is well settled, however, that he must allege in his bill in equity that such a request has been made and has not been complied with.⁴ There has been considerable discussion as to

holding that the attorney-general is not a necessary party defendant. *Cf. Ryan v. Ray*, 33 Alb. L. J. 321 (Ind. 1886). Sometimes the directors of another corporation are proper parties defendant. See *Terhune v. Midland R. R. Co.*, 38 N. J. Eq. 423 (1884). A person may be made a party defendant for purposes of discovery only. See *Lewis v. St. Albans, &c., Works*, 50 Vt. 477 (1878).

¹ *Winsor v. Bailey*, 55 N. H. 218 (1875).

² *Salomons v. Laing*, 12 Beav. 339 (1849).

³ *Thomas v. Hoblen*, 8 Jur. N. S. 125 (1862). And see in general on multifariousness herein, *Merchants, &c., Line v. Waganer*, 71 Ala. 581; *Smith v. Rathbun*, 22 Hun, 150 (1880).

⁴ *Cogswell v. Bull*, 39 Cal. 320 (1870); *Hazard v. Durant*, 11 R. I. 195 (1875), the court saying that the allegations of request "will be sustained by proof of a request to the stockholders in corporate meeting, or to the directors in office when the suit began, or in any other mode, so that it be in legal effect a request to the corporation." *Talbot v. Scripps*, 31 Mich. 268 (1875), where Mr. Justice Cooley

says: "The wrong alleged will be seen to be a corporate wrong, in which all the stockholders are proportionally interested, and any legal redress should be at the instance of the corporation, if the board of directors will consent to demand it. There is no allegation that the board has been requested to bring suit and has refused. Under the circumstances we know of no ground on which the suit can be maintained. As well might an individual stockholder bring suit to recover his share of corporate funds which had been lost by negligence or embezzlement, or his proportion of insurance money on the corporate property destroyed by fire. The injury counted on is not a separate injury to each of the stockholders, but a joint injury to all, and the corporation represents all for the purposes of legal remedy; at least until it is shown that the corporate authorities refuse after proper application to act." *Ware v. Bazemore*, 58 Ga. 316 (1877); *Merchants, &c. Line v. Waganer*, 71 Ala. 581; *Hersey v. Veazie*, 24 Me. 9 (1844); *Memphis City v. Dean*, 8 Wall. 64 (1868); *House v. Cooper*, 30 Barb. 157 (1858); *Abbott v. Merriam*, 62 Mass. 588 (1851); *Morgan*

whether the stockholder, in addition to his request to the corporate officers to institute the suit, should not also be required to attempt to induce the stockholders in meeting assembled to take action by directing the directors to bring suit, or by refusing to re-elect them at the next election. The facts, however, that the stockholders in meeting assembled cannot control the discretion of the directors in bringing such a suit; that the remedy of refusing to re-elect them involves delay, and the assumption that a majority of the stockholders can by the election control such a suit; that irreparable injury or the vesting of great financial interests may occur in the meantime; and that laches may arise as a bar to the stockholder's suit, have settled the rule that the stockholder's request to the corporate directors to institute the suit is sufficient. He need not also apply to a stockholders' meeting.¹ In the Federal courts the necessity of an allegation that the corporation has been requested to sue and has refused, is fixed by a rule of the court.²

v. R. R. Co. 29 Vt. 545 (1851). But a request to bring the suit in a Federal court is insufficient. See *Newby v. Oregon Central R. R. Co.*, 1 Sawyer, 63 (1870). The leading case, *Foss v. Harbottle*, 2 Hare, 461 (1843), failed by reason of a failure to make this effort to induce the corporation to act. In the important case *Greaves v. Gouge*, 69 N. Y. 154 (1877), the court said that "an action for injuries caused by such misconduct must be brought in the name of the corporation, unless such corporation or its officers, upon being applied to for such a purpose by a stockholder, refuse to bring such action. In that contingency and then only can a stockholder bring an action for the benefit of himself and others similarly situated, and in such an action the corporation must necessarily be made a party defendant. When a stockholder brings such an action the complaint should allege that the corporation on being applied to refuses to prosecute; and as this averment constitutes an essential element of the course of action the complaint is defective and insufficient without it." *Cogswell v. Bull*, 39 Cal. 320 (1870), where the court said: "So long as the corporation is willing to perform its duty towards its stockholders by instituting and conducting in good faith the necessary legal proceedings to recover money misapplied by the trustees, the stock-

holders have no cause to complain; but if the corporation, after a proper demand, refuses to institute the action, the stockholders may sue in their own names. If it were otherwise there would be a failure of justice and a great many of the stockholders might go without redress. It is, therefore, necessary in an action by a stockholder in such cases to aver a demand and refusal, without which the action will not be sustained." The defendant cannot raise this point in the appellate court for the first time. See *Bulkeley v. Beg, &c., Co.*, 77 Mo. 105 (1882). The request to the directors must be made in good faith and the refusal must be real and not collusive. *Bacon v. Irvine*, 11 Pac. Rep. 646 (Cal. 1886).

¹ *Mason v. Harris*, L. R. 11 Ch. D. 97 (1879), holding also that the court has no power to order such a meeting. See a discussion of this question in *Brewer v. Boston Theatre*, 104 Mass. 378 (1870). See also *Gregory v. Patchett*, 33 Beav. 595 (1864).

² Rule 94 " . . . It [the bill] must also set forth with particularity the efforts of the plaintiff to secure such action as he desires on the part of the managing directors or trustees, and, if necessary, of the shareholders and the causes of his failure to obtain such action." *McHenry v. N. Y., &c. R. R. Co.*, 22 Am. & Eng. R. R. Cas. 50. See *Leo v. Union*

§ 695. *When such an allegation may be omitted.*—There are occasions when the allegation that the stockholder has requested the directors to bring suit and they have refused, may be omitted, since the request itself is not required. This occurs when the corporate management is under the control of the guilty parties. No request need then be made or alleged, since the guilty parties would not comply with the request, and even if they did the court would not allow them to conduct the suit against themselves.¹ Nevertheless, instead of this allegation the complainant must allege the facts which excuse such a demand or request to the directors, and these facts must be stated with particularity and definiteness.²

§ 696. *Miscellaneous allegations of the complainant.*—The allegations which set forth the complaining stockholder's cause of action will depend largely of course on the particular facts of each case. It is necessary, however, to determine first, whether the allegations are to make out a case of fraud, or of an *ultra vires* act, or of a negligent act. If an *ultra vires* act is complained of, the gist of the action is not fraud, and it need not be alleged.³ But where the action is to remedy a fraud, the allegations must clearly charge to that effect. The word "corrupt" has been held insufficient herein.⁴ If the action is to set aside an *ultra vires* act, the act itself must be stated with particularity.⁵

Pacific Ry. Co., 19 Fed. Rep. 283 (1884); Converse v. Dimock, 6 Am. & Eng. Corp. Cas. 418 (1884); Bill v. Western Union Tel. Co. 16 Fed. Rep. 14; Foote v. Cunard Min. Co. 17 Id. 46 (1883), holding that an allegation that the corporation would probably refuse relief is insufficient.

¹ Brinckerhoff v. Bostwick, 88 N. Y. 52; Rogers v. Lafayette, &c. Works, 52 Ind. 295 (1875); County of Tazewell v. Farmers, &c. Co. 12 Fed. Rep. 752 (1882); Board of Tippecanoe Co. v. Lafayette, &c. R. R. Co., 50 Ind. 85 (1875); Wilcox v. Brickel, 11 Neb. 154 (1881), where the officers had absconded; Currier v. N. Y., &c. R. R. Co., 35 Hun, 355 (1885); Ramsey v. Gould, 57 Barb. 398 (1870); Kelsey v. Sargent, 40 Hun, 150 (1886); Parrott v. Byers, 40 Cal. 614 (1871); Fisher v. Andrews, 37 Hun, 176; Heath v. Erie Ry. Co., 8 Blatch. 347 (1871), the court saying: "It would be a mockery to require or permit a suit against them to be brought and prosecuted under their management to obtain the relief sought by

this bill." *Mussina v. Goldthwaite*, 34 Texas, 125 (1870); *Dowd v. Wisconsin, &c. R. R. Co.*, 65 Wis. 108 (1886); *Pond v. Vermont, &c. R. R. Co.*, 12 Blatch. 280 (1874). But an allegation that the management is under the control of persons appointed by the guilty parties is insufficient. See *McMurray v. Northern, &c. Ry. Co.*, 22 Grant (U. C.), 476 (1875). And an allegation that the directors are "nearly if not entirely" in league with the guilty parties is insufficient. *Cogswell v. Bull*, 39 Cal. 320 (1870).

² See cases in preceding note. The stockholder may bring his suit although the corporation has been dissolved. *Lafayette Co. v. Neely*, 21 Fed. Rep. 738 (1884).

³ *Clinch v. Financial Co.*, L. R. 5 Eq. 450, 482 (1868).

⁴ *Russell v. Wakefield, &c. Co.*, L. R. 20 Eq. 474 (1875).

⁵ *Leo v. Union, &c. Ry. Co.*, 19 Fed. Rep. 283 (1884).

§ 697. *Prayer for relief.*—The relief for which prayer is made in the bill will depend upon the character of the act complained, and also of the facts in the particular case. Generally it is to compel the director or third parties to pay over to the corporation money or property fraudulently held by the defendants, or to enjoin acts, or to set aside transactions, or for a receiver, or for dissolution, or for more than one of these. It is well settled that the prayer for relief may be in the alternative.¹ The relief granted cannot exceed that which is asked.²

§ 698. *Property received under the act objected to must be returned upon that act being set aside.*—This is a principle of law that applies to all the remedies given by a court of equity in remedying the frauds or *ultra vires* acts of the directors or third persons against the corporation. He who seeks equity must do equity. An *ultra vires* act will not be set aside unless the money or property received by the corporation from third persons thereby is returned to such persons.³

§ 699. *Injunction restraining the corporate officers and others from doing specified acts.*—The ordinary remedy of the stockholder is an injunction by a court of equity restraining the corporate officers from doing the specified fraudulent or *ultra vires* act which the stockholder complains of.⁴ Generally the injunction runs to the corporation itself, and this is sufficient to make it effectual and binding upon all corporate officers to whose notice it comes.⁵

§ 700. *Injunction against corporate officers acting at all, and the appointment of a receiver.*—The law is well settled that the courts have no power to remove corporate officers.⁶ Nor

¹ Colton v. Ross, 2 Paige, 396 (1831); Thomas v. Hobler, 4 De G., F. & J. 199 (1861).

² Latimer v. Eddy, 46 Barb. 61 (1864).

³ Buford v. Keokuk, &c., Co., 69 Mo. 611 (1879); Harpending v. Munson, 91 N. Y. 650 (1885). Cf. Gray v. N. Y., &c., Co., 5 T. & C. 224 (1875).

⁴ River Dun Nav. Co. v. North, &c., Ry. Co., 1 Ry. Cas. 184, 153 (1838); Blatchford v. Ross, 54 Barb. 42 (1869).

⁵ See § 692, *supra*. Also Hatch v. Chi-

cago, &c., R. R. Co., 6 Blatch. 105 (1868); Trimmer v. Penn. &c., R. R. Co., 36 N. J. Eq. 411 (1883), holding, however, that the officers are not liable herein for contempt by reason of the acts of sub-contractors. See People v. Sturtevant, 9 N. Y. 263 (1853); Id. v. Pendleton, 64 N. Y. 622 (1876).

⁶ Neall v. Hill, 16 Cal. 145 (1860), the court saying: "It is well settled that there is no jurisdiction in equity with regard to the removal of corporate officers of any description."

can the stockholders, in meeting assembled, remove the officers.¹ It is also well established that a court of equity cannot practically remove corporate officers by enjoining them from performing any of their customary duties, and by appointing a receiver to manage the corporate affairs.² Frequently, however, the power to restrain or remove corporate officers, and to appoint a receiver

¹ *Imperial, &c., Co. v. Hampson*, 1882, W. N. 189. See § 627.

² *People v. Albany, &c., R. R. Co.*, 55 Barb. 344, 383 (1869); *Einstein v. Rosenfield*, 38 N. J. Eq. 309 (1884), where the court said: "The general jurisdiction of equity over corporate bodies does not, in the absence of express statutory authority, extend to the power of dissolving the corporation, or of winding up its affairs and sequestrating the corporate effects and property; and courts of equity will not, ordinarily, by virtue of their general equitable jurisdiction or of their visitatorial powers over corporate bodies, sequester the effects of the corporation, or take the management of its affairs from the hands of its own officers, or intrust it to the control of a receiver of the court, upon the application either of creditors or shareholders." *Howe v. Deuel*, 43 Barb. 504 (1865); *Waterbury v. Merchants, &c., Co.*, 50 Barb. 157 (1867), where the court said: "The infidelity or misconduct of some, or even of all, of the trustees or managers of such an association, affords no grounds for taking away the rights of the shareholders who constitute the company, either by dissolving it or taking away its management and placing it in the hands of an officer of the court. In such a case the principles of remedial or preventative justice go no further than to enjoin or forbid the misconduct or remove the unfaithful officer." *Cicotte v. Anciaux*, 53 Mich. 227 (1884); *La Grange v. State Treas.*, 24 Mich. 468 (1872), where the court said: "It is not within the power of any court, except in proceedings to divest the corporation of its charter franchises, to take away the management of its affairs from the hands of the directors lawfully invested with that management, and give it into the hands of other managers. The corporate functions must be performed by corporate officers." In *Hyde Park Gas Co. v. Kerber*, 5 Bradw. (Ill.) 132 (1879), where a decree had been made that a receiver be appointed unless the officers paid over money received by them in fraud of corporate

rights, the court set aside the decree, and said: "In principle this is very much like sending the creditor to jail because his debtor cannot pay him, and is so opposed to that spirit of justice which pervades all the true doctrines of equity jurisprudence, that it will not bear discussion." *Bayless v. Orme*, Freeman's Ch. (Miss.) 161 (1841); *People v. Conklin*, 5 Hun, 452 (1875); *Hand v. Dexter*, 41 Ga. 454 (1871); *Baker v. Adm'r of Backus*, 32 Ill. 79 (1863); *People v. Albany, &c., R. R. Co.*, 7 Abb. Pr. N. S. 290; *Belmont v. Erie Ry. Co.*, 52 Barb. 637 (1869); *Smith v. Wells*, 20 How. Pr. 168. Even where two rival boards of directors are litigating their respective rights, the court cannot turn the corporate affairs over to a receiver. See *Karnes v. Rochester, &c., R. R. Co.*, 4 Abb. Pr. N. S. 107 (1867), where the court said: "This contest does not, in my judgment, give the court any authority or furnish any ground for it to step in, in the meantime, and take charge of the affairs of the corporation, and perform the duties of its existing legal board of directors." See *Gavenstine's Appeal*, 49 Penn. St. 310 (1865), holding that the appointment of a receiver is equivalent to enjoining the officers from managing the corporate business. A few cases have held that the court, under extreme circumstances, may appoint a receiver to take charge of the corporate business, even though the corporation is solvent, and no dissolution is intended, and no corporate creditors' interests are involved. See *Stevens v. Davison*, 18 Gratt. (Va.) 819 (1868), where a railroad was turned over to a receiver to protect stockholders' rights. *Frostburg Bldg. Assn. v. Stark*, 47 Md. 338 (1877). In the case of *Hayward v. Lincoln Lumber Co.*, 26 Northwest. Rep. 184 (Wis., 1885), the corporation was insolvent. In *Lawrence v. Greenwich Fire Ins. Co.*, 1 Paige, 587 (1829), the court appointed a receiver to preserve the corporate property, there having been no officers elected by the stockholders. See also *Conro v. Gray*, 4 How. Pr. 166.

of the corporation, is given to the court by a statutory enactment.¹

§ 701. *Miscellaneous remedies.*—It has been held and clearly established that a stockholder cannot bring about the dissolution of the corporation merely because the officers have been guilty of a breach of trust.² Nor can he defeat an action for his subscription by alleging such a defense.³

§ 702. *The complaining stockholder controls the conduct of the suit.*—It is a principle of equity practice, when a person brings a suit in behalf of himself and such others as may wish to come in, who are similarly situated, that the complaining stockholder controls the case, and may continue, compromise, abandon, or discontinue it at his pleasure.⁴ In case the suit is successful, the complaining stockholder is entitled to have his costs paid by the corporation.⁵

§ 703. *No contribution among the directors.*—There is no contribution among directors guilty of a breach of trust, for which a part are held liable.⁶

¹ In New York it would seem, under § 1810 of the Code of Civil Procedure, that a receiver cannot be appointed at the instance of a stockholder suing to remedy the frauds, *ultra vires* acts, or negligence of a director. See also *Verplanck v. Mercantile Ins. Co.*, 1 Edw. Ch. 83 (1831). In New York it has been held that a stockholder may have a corporate officer arrested for his frauds on the corporation. *Crook v. Jewett*, 12 How. Pr. 19 (1854).

² See § 632, *supra*.

³ See § 187, *supra*. Also *Chetlain v. Republic Life Ins. Co.*, 86 Ill. 220 (1877); *South Georgia, &c., R. R. Co. v. Ayres*, 56 Ga. 230 (1876). Nor can the stockholder enjoin a call. *Ex parte Booker*, 18 Ark. 338 (1857). If an illegal consolidation is set aside, the stockholder, of the new company may recover back the amount paid in by them. *In re Bank of Hindustan*, L. R. 16 Eq. 417 (1873).

⁴ "The plaintiff, as he acts upon his own mere motion, and at his own expense, retains (as in other cases) the absolute dominion of the suit until decree, and may discuss the bill at his pleasure; after decree, however, he cannot by his conduct, deprive other persons of the same

class of the benefit of the decree, if they think fit to prosecute it." 1 Daniel's on Ch. Pl. & Pr. (4th Am. ed.) 244; *Allen v. N. J. Southern R. R. Co.*, 49 How. Pr. 14 (1875), where the court said: "Actions like the present one may be discontinued, settled, or compromised by the plaintiff at any time before judgment, nor could any other stock prevent such result. Nor would such settlement or compromise prevent a suit by the corporation itself hereafter, for the same objects and results as are contemplated by this action, unless made a party to this proceeding, by the final determination of which, on the merits, it would be concluded and truly bound." But see *Seaton v. Grant*, L. R., 2 Ch. 459 (1867). *Cf. Searth v. Chadwick*, 14 Jur. 300 (1849). In the case *Belmont v. Erie Ry. Co.*, 52 Barb. 637 (1869), the court held that the other stockholders could interfere in the management of the case.

⁵ *Central R. R. Co. v. Pettus*, 113 U. S. 116 (1885). *Cf. In re Atty.-Gen. v. North, &c., Ins. Co.*, 91 N. Y. 57 (1883).

⁶ *Wilkinson v. Dodd*, 40 N. J. Eq. 123 (1885); *Peck v. Ellis*, 2 Johns. Ch. 131 (1816). See *Power v. Conner*, 19 W. R. 923.

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